HSBC UK Bank plc

Annual Report and Accounts 2019

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Presentation of information

This document comprises the Annual Report and Accounts 2019 for HSBC UK Bank plc ('the bank') and its subsidiaries (together 'HSBC UK' or 'the group'). 'We', 'us' and 'our' refer to HSBC UK Bank plc together with its subsidiaries. It contains the Strategic Report, the Report of the Directors, the Statement of Directors' Responsibilities and Financial Statements, together with the Independent Auditors' Report, as required by the UK Companies Act 2006. References to 'HSBC Group' or 'the Group' within this document mean HSBC Holdings plc together with its subsidiaries.

HSBC UK is exempt from publishing information required by The Capital Requirements Country-by-Country Reporting Regulations 2013, as this information is published by its ultimate parent, HSBC Holdings plc. This information will be available in June 2020 on the Group's website: www.hsbc.com.

Pillar 3 disclosures for HSBC UK are also available on www.hsbc.com, under Investor Relations.

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

Our reporting currency is £ sterling. Unless otherwise specified, all $ symbols represent US dollars.

Cautionary statement regarding forward-looking statements

This *Annual Report and Accounts 2019* contains certain forward-looking statements with respect to the financial condition, results of operations and business of the group.

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

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

Key financial metrics

	Year ended		Half Year	
	31 Dec 2019	31 Dec 2018[1]	**31 Dec 2019[1]**	30 Jun 2019[1]
Reported results				
Reported revenue (£m)	**6,484**	3,357	**3,169**	3,315
Reported profit before tax (£m)[3]	**1,010**	1,064	**394**	616
Reported profit after tax (£m)	**516**	763	**165**	351
Profit attributable to the shareholders of the parent company (£m)	**512**	763	**164**	348
Return on average tangible equity (annualised) ('RoTE') (%)[3]	**2.4**	8.8	**N/A**	N/A
Net interest margin (%)	**2.05**	2.22	**N/A**	N/A
Expected credit losses and other credit impairment charges ('ECL') as % of average gross loans and advances to customers (%)	**0.34**	0.35	**N/A**	N/A
Adjusted results				
Adjusted revenue (£m)	**6,613**	3,352	**3,298**	3,315
Adjusted profit before tax (£m)[3]	**2,263**	1,299	**1,125**	1,138
Cost efficiency ratio (%)[3]	**56.5**	52.1	**57.4**	55.7
Adjusted return on average tangible equity (annualised) ('RoTE') (%)[2, 3]	**9.9**	11.7	**N/A**	N/A
Balance sheet				
Total assets (£m)	**257,102**	238,939	**N/A**	N/A
Net loans and advances to customers (£m)	**183,056**	174,807	**N/A**	N/A
Customer accounts (£m)	**216,214**	204,837	**N/A**	N/A
Average interest-earning assets (£m)	**231,701**	219,419	**N/A**	N/A
Loans and advances to customers as % of customer accounts (%)	**84.7**	85.3	**N/A**	N/A
Total shareholders' equity (£m)	**22,191**	22,273	**N/A**	N/A
Tangible ordinary shareholders equity (£m)	**16,001**	16,243	**N/A**	N/A
Capital, leverage and liquidity				
Common equity tier 1 ('CET1') capital ratio (%)[3]	**13.0**	12.7	**N/A**	N/A
Total capital ratio (%)	**19.2**	18.3	**N/A**	N/A
Risk-weighted assets ('RWAs') (£m)	**85,881**	91,839	**N/A**	N/A
Leverage ratio (%)	**5.0**	5.6	**N/A**	N/A
High-quality liquid assets (liquidity value) (£m)	**56,822**	46,357	**N/A**	N/A
Liquidity coverage ratio (%)	**165**	143	**N/A**	N/A

1 *HSBC UK's banking operations commenced on 1 July 2018, following the transfer of the qualifying businesses and subsidiaries from HSBC Bank plc. Results for the year ended 2019 have been provided on a half year to date basis in order to provide better comparability to the 2018 results. Balance sheet data and related metrics are not provided on this basis.*

2 *In the event that the current IAS 19 Pension fund surplus was zero, additional CET1 capital would be required to be held and Adjusted RoTE would be 11.3% (2018: 13.7%); we refer to this as Pension Adjusted RoTE.*

3 *These metrics are tracked as Key Performance Indicators of the group.*

Presentation of non-GAAP measures

In measuring our performance, the financial measures that we use include those derived from our reported results in order to eliminate factors that distort period-on-period comparisons. Such measures are referred to as adjusted performance. A reconciliation of reported to adjusted performance is provided on pages 11 to 14.

RoTE is computed by adjusting the reported equity for goodwill and intangibles. A reconciliation is provided on page 119, which details the adjustments made to the reported results and equity in calculating RoTE.

About us

HSBC UK comprises of Retail Banking and Wealth Management ('RBWM'); Commercial Banking ('CMB'), Private Banking ('PB') and a restricted Global Banking and Markets ('GB&M') business.

HSBC UK is strongly connected to the rest of the HSBC Group and leverages this network to support customers and grow revenue across key trade corridors around the world.

Purpose, values and ambition

HSBC Group's purpose

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

Our values

Our values define who we are as an organisation:

Dependable

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

Open

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

Connected

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

Our UK ambition

Deeply rooted in the UK and providing a unique gateway to the world. We are investing in growth and innovation to make banking simple, safe and sustainable, and be the bank of choice for our customers, colleagues and communities through the generations.

What we do

HSBC UK, headquartered in Birmingham, has over 15 million active customers, with 22,000 colleagues across the country, supported by a further 10,000 colleagues based in our service company HSBC Global Services (UK) Limited, who provide services to HSBC UK and the wider HSBC Group.

HSBC UK manages its products and services through four businesses: RBWM, CMB, PB and a restricted GB&M business. In addition, certain central operations of the HSBC UK business lines are managed through the Corporate Centre.

Retail Banking and Wealth Management

Customers

RBWM serves over 14 million active customers under four brands: HSBC UK, first direct, M&S Bank and John Lewis Financial Services ('JLFS'). As well as catering for the mass retail market, we also provide services for emerging affluent to upper affluent individuals under the following propositions: HSBC UK Advance, HSBC UK Premier, and Jade by HSBC UK Premier.

Products and services

We offer a comprehensive set of banking products and services to support retail customers' everyday banking needs through a selection of channels, including branch, telephony and digital. We offer full banking services, mortgages, unsecured lending, wealth solutions and general insurance.

Commercial Banking

Customers

CMB serves over 830,000 active customers across the UK, ranging from start-ups to multi-national corporates, through four customer groups: Large Corporates ('LC'); Mid-Market Enterprises ('MME'); Business Banking ('BB'); and Small Business Banking ('SBB').

Products and services

CMB supports customers with tailored financial products and services to allow them to operate efficiently and to grow, with a strong relationship focus. These include Credit and Lending, Global Liquidity and Cash Management (GLCM), and Global Trade and Receivables Finance (GTRF). Through close collaboration with HSBC Group, we can make available GB&M products and Securities Services to our customers.

Private Banking

Customers

PB serves high and ultra-high net worth individuals and families; including those with international banking needs.

Products and services

PB supports clients with investment management; including advisory, discretionary and brokerage services. We also offer private wealth solutions, comprising trusts and estate planning, designed to protect wealth and preserve it for future generations. This is as well as a full range of lending and transactional banking services.

Global Banking and Markets

We are able to offer selected GB&M products to our customer base. For example, we maintain a markets team that help to support the sale of eligible markets products to our CMB customers from HSBC Bank plc.

Corporate Centre

Corporate Centre comprises Central Treasury, including Balance Sheet Management, interests in a joint venture, and central stewardship costs that support our businesses.

Economic background and outlook

Real quarterly UK GDP growth slowed from 0.5% in the third quarter of 2019, to 0.0% in the fourth quarter, according to data from the Office of National Statistics. The underlying pace of UK economic growth remains subdued, with full-year growth at 1.4% for 2019.

The labour market remains relatively firm with the unemployment rate standing at 3.8% in the three months to November. The annual rate of inflation, according to the Consumer Price Index ('CPI'), stood at 1.3% in December 2019. The 'core' CPI rate, which strips out food and energy prices, stood at 1.4%.

Following the general election on 12 December, the UK's political landscape has changed substantially. With a large majority in Parliament, the government presided over the UK's withdrawal from the European Union (EU) on 31 January. After a transition period lasting until the end of 2020, the UK is set to move to a new trading relationship with the EU.

Still some uncertainty remains. Firstly, it remains to be seen what form the UK's future relationship with the EU, and other trading partners, will take. Secondly the government is yet to outline its fiscal plan in detail, which will be set out in the March budget. Whilst business surveys point to a post-election boost to economic growth, it is unclear how large and sustained this will be.

Given these continued uncertainties, HSBC Research maintains a cautious outlook. It forecasts below-average GDP growth of 1.1% in 2020, then an acceleration to 1.4% in 2021, driven, in part, by looser fiscal policy. Despite this, the subdued outlook is unlikely to deliver much inflationary pressure. HSBC Research also forecasts the Bank Rate to be reduced from 0.75% to 0.50% in the first half of this year, then to remain on hold until at least the end of 2021.

Process of UK withdrawal from the European Union

The UK left the EU on 31 January 2020, and entered a transition period until 31 December 2020. During the transition period the UK will continue to be bound by EU laws and regulations. Beyond that date, there is no certainty on what the future relationship between the UK and the EU will be. This creates market volatility and economic risk, particularly in the UK. We will continue to work with regulators, governments, our customers and colleagues to manage the risks resulting from the UK's exit from the EU as they arise, particularly across those industry sectors most impacted. For more information please refer to pages 18 and 22 of the Report of the Directors.

Our strategy

The launch of the HSBC Group's ring-fenced bank (HSBC UK) in 2018, marked the beginning of a new chapter for HSBC's strategy in the UK. This has been built around four strategic priorities: customer experience, colleague engagement and shareholder value growth, all underpinned by simplification of the business.

Customer experience

We are investing in digital capabilities to enhance the overall customer experience, whilst also launching new initiatives to support our customers.

Progress in 2019

We have made good progress in improving customer experience across our brands and businesses. first direct achieved top spot in the Competition and Markets Authority ('CMA') rankings for customer service in February 2020. HSBC UK RBWM also showed significant improvements, moving from twelfth to joint sixth. CMB moved to second place in the most recent Savanta (previously Charterhouse) survey whilst we also saw an improvement in our annual Private Banking relationship survey, with scores increasing by 0.3 points to 8.1 out of 10. For more information on customer service and satisfaction measures, please refer to page 9.

This progress reflects our continued focus on enhancing the customer experience, including the integration of features from our Connected Money proposition into our mobile app and the beta test of HSBC Kinetic for business customers. We also launched our 'Intrepid Exporters' campaign in CMB as well as a new £14bn Small and Medium Enterprise ('SME') lending fund, our largest to date, as part of our commitment to help British businesses navigate the UK's withdrawal from the EU and realise their ambitions for growth. This is reflected in our ranking of joint third for SME overdraft and loan services within the February 2020 CMA rankings.

Financial inclusion and vulnerability has also been a key focus for HBSC UK, with the launch of the Survivor Bank and No Fixed Address initiatives in 2019. For more information on how we have supported financial inclusion please refer to page 5.

Future focus

We plan to focus on accelerating digital developments to drive customer growth across our businesses with the aim of improving the customer experience. We aim to focus on leveraging our multi-brand strategy within RBWM to acquire new customers as well as improving our penetration of MMEs within our CMB business through a renewed focus on being where the growth is.

Colleague engagement

We are building an inclusive culture with a greater focus on colleagues' wellbeing.

Progress in 2019

According to internal measures, colleague engagement improved in 2019, with the metric 'I would recommend HSBC as a great place to work" increasing by 2 percentage points to 62% (vs FY18). With a focus on mental health and wellbeing, we held a number of wellbeing events throughout the year and hosted our first wellbeing month in May which saw over 2,500 colleagues attend events. Over 400 colleagues also voluntarily undertook 'mental health conversation skills in practice' training throughout 2019.

Future focus

We plan to build on the progress made in 2019, ensuring that our colleagues continue to feel empowered. Wellbeing, mental health, career development and pride will remain key priorities.

Shareholder value growth

Responding to emerging customer needs, we aim to grow our business in a safe and sustainable way. This will include us targeting growth in market share for mortgages and commercial lending.

Progress in 2019

Customer numbers have grown across RBWM, whilst combined customer numbers in our LC and MME customer groups in CMB remained broadly flat. We also leveraged relationships across business lines, with over 330 customers referred into PB from RBWM and CMB.

Despite a challenging environment, HSBC UK maintained revenues and grew loans and advances balances, with mortgage balances increasing by 7.1% to £101bn and commercial lending balances increasing by 1.7% to £68bn. We grew our mortgage market share by 0.3% to 6.8%, whilst our commercial lending market share remained broadly flat at 9.9%[1].

Reported profit has been impacted by an increase in operating expenses, this is primarily due to an increase in customer remediation, including a £932m increase in PPI provisions. Adjusted return on tangible equity ('RoTE') was 9.9% (Pension Adjusted RoTE was 11.3%).

For more information on our financial performance in 2019, please refer to pages 10 to 15.

1 Loans and overdraft balances as a percentage of the market.

Future focus

We aim to continue to grow our mortgage market share, through controlled expansion of the intermediary channel, as well as our commercial lending market share, whilst maintaining a conservative risk appetite. We aim to grow revenue as we invest in the business and are committed to a positive adjusted jaws (year-on-year revenue growth % higher than cost growth %) discipline in the medium term.

Simplification

We are enhancing and simplifying our business to enable and empower our colleagues to support our customers.

Progress in 2019

We continually strive to simplify our organisation and in 2019 we delivered efficiencies in key on-boarding journeys, with mortgage time-to-offer reducing to 9 days from 12 days and relationship managed CMB segment on-boarding times decreasing by 30%, vs December 2018. We have also removed complexity by eliminating scarcely used products in RBWM and CMB, whilst also saving time for our colleagues by optimising internal governance.

Work was ongoing throughout 2019 for the transfer of nearly all of HSBC Private Bank (UK) Limited's business to the bank. This was effected by way of a court sanctioned transfer scheme under Part VII of the Financial Services and Markets Act 2000, and was completed on 1 January 2020. The transfer is anticipated to enhance the collaboration between RBWM, CMB and PB, helping to improve the customer lifecycle experience. Closer alignment will also provide PB with access to digital and technology developments.

Future focus

We aim to simplify our back office systems and processes to support our colleagues and utilise new and emerging technologies where possible to help improve customer service and cost efficiency.

Our core advantages

Full banking capability

We serve customers ranging from individual savers through to large multinational corporations with the support of our four businesses. Our full banking capability assists us in seeking to meet our customers' diverse financial needs, reduce our risk profile and volatility, and generate stable returns for shareholders.

Value of our network and access to an exceptional global presence

Within the UK we provide products and services digitally, by phone and face-to-face through over 650 branches, bureaux and offices, 64 commercial centres, and 4 contact centres.

For customers with international interests, we are intrinsically connected with the HSBC Group's wider global network, enabling our customers to seize international growth opportunities. This helps us build deeper and more enduring relationships with businesses and individuals. The HSBC Group's geographic reach and network of customers also allows greater insight into the trade and capital flows across supply chains.

Business synergies

We share resources and product capabilities across our businesses and leverage these synergies when serving our customers. For example, the foreign exchange and wealth management needs of RBWM customers create opportunities for GB&M. CMB collaborates closely across HSBC UK to fully support our customers at various points in their lifecycle; for example, PB can support the owners of CMB companies looking to exit and grow their wealth, and CMB works closely with RBWM to offer colleague banking services for our customers.

How we do business

We conduct our business in a way that seeks to ensure we support the sustained success of our customers, colleagues and communities. We see investment in our capabilities and processes as a source of remaining sustainable in the long-term.

Supporting our customers

We create value by providing the products and services our customers need and aim to do so in a way that fits seamlessly into their lives. This helps us to build long-lasting relationships with our customers. We build trust by striving to protect our customers' data and information, and delivering fair outcomes for them. If things do go wrong, we address complaints in a timely manner.

How we listen

We listen to our customers in a number of different ways, including through our interactions with them, surveys, social media and through their complaints. We use these insights to improve our services.

When things go wrong

To improve our services we must be open to feedback and acknowledge when things go wrong. We listen to complaints to address customers' concerns and understand where we can improve processes, procedures and systems. We focus on colleague training and emphasise the importance of recording complaints. This improves our complaint handling expertise and helps ensure our customers are provided with fair outcomes. Complaints are also monitored and reported to governance forums.

Taking responsibility for the experiences we deliver

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

Building financial inclusion and accessibility

At HSBC UK we are committed to offering support to those who, are in many cases, excluded from the banking system. In 2019, we launched our Survivor Bank initiative, which supports victims of human trafficking and modern-day slavery, with over 320 accounts opened in 2019. We also launched our 'No Fixed Address' initiative supporting the homeless and people with no fixed address, with over 90 accounts opened in 2019, with both initiatives being live in 32 branches.

We are supporting victims of financial abuse by implementing the Financial Abuse Code of Practice into UK procedures, and launching a national sort code for survivors of financial abuse. To support in the delivery of our Financial Inclusion and Vulnerability (FIV) programme, a robust internal and external campaign has been created to drive a culture change and bring FIV awareness to the forefront for our colleagues, when both serving customers or developing our products and journeys. This is reinforced by our specialist team who provide support to our customers in vulnerable circumstances.

Supporting our colleagues

Our colleagues span many cultures and communities. By focusing on colleague well-being, diversity, inclusion and engagement, as well as building our colleagues' skills and capabilities for now and for the future, we aim to create an environment where our colleagues can fulfil their potential. We want to have an open culture where our people feel connected, supported to speak up and where our leaders encourage feedback.

Creating an inclusive environment

We aim to create a working environment that is diverse and inclusive, where everyone feels they can thrive. We encourage diversity of thought from all of our colleagues so we can deliver on our ambition and believe continued success will require a workforce that reflects our customers and the communities we serve.

Our definition of diversity and inclusion goes broader than inherent characteristics to include other differences that make individuals unique, such as cultural fluency, global experience and work styles.

Gender balance is an important part of creating a diverse and inclusive environment. HSBC UK supports the 30% Club, which strives for a target of 30% women in senior leadership roles

(classified as 0-3 in our global career band structure) by the end of 2020. HSBC UK achieved a figure of 32% in 2019.

More information about our diversity and inclusion activity and our UK Gender Pay Gap Report is available at www.hsbc.com.

Listening to our colleagues

It is vital we understand how our colleagues feel as it helps us give them the right support to thrive and serve our customers well. We capture their views on a range of topics, such as our strategy, culture, behaviour, well-being and working environment, through our colleague survey, Snapshot, which runs twice yearly. Results are presented to the HSBC UK Executive Committee, the Board of Directors of HSBC UK ('the Board'), and other relevant committees of the functions and businesses. This ensures the attitudes and sentiments of our colleagues inform decision-making at all levels of HSBC UK, and action can then be taken to tackle areas of concern. Additionally, we also participate in the external Banking Standards Board Annual assessment, comprising a colleague survey and focus groups where our colleagues can also have their say.

We have a structured communications approach that uses leadership communications, campaigns and a regular flow of news to help colleagues to serve our customers better, make sense of our strategy, focus on our commercial priorities and provide clarity on issues. We build a sense of pride and purpose by recognising our colleagues' contributions to our business and celebrating the achievements of HSBC UK.

Empowering a speak up culture

Having a culture where our colleagues feel able to speak up is critical. Individuals are actively encouraged to raise concerns about wrongdoing or unethical conduct and multiple channels, including telephone hotlines, online and email, have been established to support this.

HSBC Confidential provides a platform that enables all colleagues to raise concerns on any issues outside of the usual escalation channels; in confidence and without fear of retaliation. Concerns raised are investigated thoroughly and independently. HSBC UK does not condone or tolerate any acts of retaliation against anyone who raises a concern.

Supporting our community

We have a responsibility to invest in the long-term prosperity of our community. In 2019, we donated £6.6m to charities and non-profit organisations, running programmes and projects in the UK.

We are committed to helping our colleagues contribute to their communities, and we encourage volunteering through paid volunteering days.

We recognise technology is developing at a rapid pace and new skills are needed to succeed. That is why we are focussed on increasing the future skills of our customers, colleagues and communities. Our initiatives also support disaster relief efforts when required.

Future skills

Our sustainability strategy focuses on three key areas of future skills: employability, entrepreneurship and financial capability.

Employability

The Prince's Trust

HSBC UK's charitable partnerships help young people develop employment related skills. The Group has supported The Prince's Trust since 2012 and we are the largest corporate partner for their employment programme. In 2019, our support enabled 1,985 young people to re-engage with education, training or employment.

In 2013, the Group started our UK Traineeship Programme, providing work experience and real job opportunities to young people supported by The Prince's Trust. In 2019 HSBC UK provided training for 36 young unemployed people, leading to 14 successful job outcomes, 11 of which gained employment directly with HSBC UK.

Entrepreneurship skills

Young Enterprise Company programme

HSBC have supported Young Enterprise for over thirty years. Our 2019 funding has supported 3,374 pupils from the most deprived areas of the UK to take part in the Company Programme.

The programme gives young entrepreneurs a live experience of starting a company and taking a product to market, making the connection between school and the preparation for the world of work. Teams of up to 25 pupils work together and develop a range of skills that will support their careers and empower the next generation of entrepreneurs:

"Young Enterprise has been such an incredible experience. As a team we have grown so close and Young Enterprise has been an incredible platform to do that. For the future we expect to go bigger and better and can't wait to see what comes next." Harriette Evans, Bath Company of the Year winners 2019

Financial capability

Young Money Centre of Excellence in Financial Education

HSBC UK are working with Young Enterprise to create 17 primary centres of excellence across England, Wales and Scotland. This will see the very first centre of excellence in Financial Education launched in Scotland.

The Centres of Excellence programme is designed to embed sustainable financial education throughout a whole school, with young people at the heart of the programme. The goal is that they leave school with the knowledge, skills and confidence to be able to make informed and independent financial decisions:

"Introducing the Centre of Excellence programme into Scotland brings a focus on high quality and sustainable financial education - something which Young Enterprise Scotland are truly committed to supporting schools to achieve. Creating a network of schools that can showcase best practise financial education and support other local schools to do the same, creates an excellent starting point from which to develop financial education further within Scotland." Geoff Leask – Chief Executive at Young Enterprise Scotland

Community investment

Our local charitable funding supports vulnerable people through the generations. In 2019, these colleague-led projects supported 25,605 people across 58 local charities. In addition, we have a fund available to allow colleagues to match fundraising or volunteering in their own time. This raised £6.9m for local charities including our matched funding.

Thousands of HSBC UK colleagues volunteer every year with our charitable partnerships and programmes. All colleagues can take two days per annum to volunteer for a charity of their choice in work time. 8,155 colleagues gave a total of 68,099 work-time hours to community activities.

Maintaining a responsible business culture

HSBC UK is a leading UK financial institution that aims to be simple, safe and sustainable; this reflects our responsibility to protect our customers, our communities and the integrity of the financial system.

At a glance

We act on our responsibility to run our business in a way that upholds high standards of corporate governance.

We are committed to working with our regulators to manage the safety of the financial system, adhering to the sprit and the letter of the rules and regulations governing our industry. In our endeavour to restore trust in our industry, we aim to act with courageous integrity and learn from past events to prevent their recurrence.

We meet our responsibility to society by paying taxes and being

transparent in our approach to this. We also seek to ensure we respect global standards on human rights in our workplace and our supply chains, and continually work to improve our compliance management capabilities.

Anti-bribery and corruption

HSBC UK is committed to high standards of ethical behaviour and operates a zero tolerance approach to bribery and corruption. We consider such activity to be unethical and contrary to good corporate governance. HSBC Group has a global Anti-Bribery & Corruption Policy which gives practical effect to global initiatives such as the Organisation of Economic Co-Operation and Development, the Convention on Combating Bribery of Foreign Public Officials in International Business Transactions and Principle 10 of the United Nations Global Compact.

Human rights

HSBC UK's commitment to respecting human rights, principally as they apply to our colleagues, our suppliers and through our lending, is set out in our 2015 HSBC Group statement on Human Rights. This statement, along with our Environmental, Social and Governance Criteria ('ESG') updates and our statements under the UK's Modern Slavery Act, are available on www.hsbc.com/our-approach/measuring-our-impact.

Engaging with our suppliers

HSBC Group have globally consistent standards and procedures for the onboarding and use of external suppliers and require suppliers to meet our compliance and financial stability requirements, as well as to keep to our sustainability code of conduct. Payment on time is of paramount importance, and as such our commitment to paying our suppliers is in line with local requirements, including the Prompt Payment Code in the UK.

More information can be found on our public website *www.hsbc.com*.

Section 172 statement

As set out in section 172 of the UK Companies Act 2006 (the 'Act'), the Directors must act in good faith to promote the success of the company for the benefit of its members as a whole. In performing their duty, under the Act, the Board is required to have full regard to, amongst other things: the interests of our colleagues; the impact of our operations on the community and environment; the need to foster the bank's business relationships with suppliers, customers and others; and the need to nurture our relationship with key stakeholders in order to maintain a reputation for high standards of business conduct and enhance the sustainable long term success of the business. The Directors give careful consideration to the factors set out above in discharging their duties.

The Directors are supported in the discharge of their duties by:

- An induction programme and ongoing training to provide an understanding of our business, financial performance and prospects;
- Management, who present proposals to the Board and Committee meetings for decision, include relevant information to enable them to determine the action that would most likely promote the success of the bank; and
- Agendas for the Board and Committee meetings are structured to provide sufficient time for the consideration and discussion of key matters.

Stakeholder engagement

Building strong relationships with our stakeholders will help achieve our ambition and promote the long term success of HSBC UK. Our stakeholders that we consider in this regard are the people who work for us, bank with us, own us, supply us and regulate us. Members of the UK Board regularly meet with bank's regulators and we proactively engage with them to facilitate strong relationships and understand the regulators' expectations that are critical to our business. Our customers' voices are heard through our interactions with them, surveys, listening to and engaging with them on social media and from their complaints. Further information on engagement with some of our stakeholders can be found on pages 6,9 and 18.

As a wholly owned subsidiary, we also benefit from certain engagement practices which take place at a HSBC Group level. For details on some of the engagement that takes place with stakeholders at the HSBC Group level, please see the HSBC Holdings plc 2019 Annual Report and Accounts and HSBC Holdings plc Environmental, Social and Governance update.

Colleague engagement

Enhancing colleague engagement is an integral part of the bank's strategy. Management, including the Chief Executive Officer ('CEO'), are actively involved in the engagement of colleagues through regular leadership calls and all colleague web-casts to keep the workforce up-to-date on business developments and answer submitted questions. The Board receives regular updates from the CEO and the Head of Human Resources on colleague matters, including feedback received through our regular external and internal colleague surveys such as the Banking Standards Board survey and internal Snapshots. During the year, Directors have also had opportunities to directly engage with local management and other colleagues.

Further details of HSBC UK's engagement with colleagues can be found on pages 4 and 6.

Consideration of stakeholders in principal decisions

The maintenance of a reputation for high standards of business conduct and the likely consequences of the Board's actions in the long-term, are taken into account in the Board's discussions and in their decision making process under section 172 of the Act. During the period, the Board received information to support its understanding of the interests and views of our key stakeholders, as appropriate, as part of the decision making process, including reports and presentations on our financial and operational performance, key performance indicators ('KPIs') on non-financial aspects of performance, including people, customers, culture and values, diversity, sustainability, risk and the outcomes of specific pieces of engagement (for example, the results of customer and colleague surveys).

The Board delegates authority for day-to-day management of the bank to the management team and engages management in setting, approving and overseeing execution of the business strategy and related policies. Management conduct much of the bank's primary engagement with both internal and external stakeholders, including regulators, with the outputs of this engagement activity providing critical insight and perspectives for the Board when taking decisions or challenging management in respect of decisions made on behalf of the bank.

Depending on the nature of the issue in question, the relevance of each stakeholder group may differ. Board decisions will not necessarily result in a positive outcome for all of our stakeholders, but by considering our purpose, values and ambition, and having due regard for stakeholder relationships, the Board aims to ensure that its decisions promote the long-term success of the bank.

The Board is responsible for reviewing the bank's strategy and approving the risk appetite statement, capital and operating plans, and dividend proposed by management. Examples of other principal decisions taken by the bank during the year include: (i) the approval of the transfer of nearly all of HSBC Private Bank (UK) Limited's business to the bank. Consideration was given to the benefits and risks of the proposed transfer, including any additional actual or contingent liabilities which could alter the bank's solvency, capital or liquidity positions; the impact on relevant stakeholders, including customers and the bank's shareholder; and regulatory implications; and (ii) the UK People Strategy and Plan. Internal and external factors considered including colleague engagement; the culture of the organisation; how we work and our organisational design; pace of automation; and demographic and generational changes.

Supporting sustainable finance

Providing the finance to help our customers transition to a low or net zero carbon economy is one of HSBC Group's key sustainable finance commitments. In 2019, we continued to expand our sustainable finance offerings across CMB, RBWM and PB.

Commercial Banking

In July 2019, HSBC UK launched a green loan proposition for our CMB customers in the UK, aligning our green loan offering to the Europe, Middle-East and Africa and Asia-Pacific Loan Market Association's ('LMA') Green Loan Principles ('GLP') published in March 2018. These aim to create market standards and guidelines, providing a consistent methodology for use across the green loan market.

The green loan proposition is available for green term loans, green revolving credit facilities and green asset finance to LCs, MMEs and SMEs. A green loan is available for a minimum amount of £300,000, enabling businesses to access finance to support their sustainability projects.

In 2017, HSBC Group announced a commitment to provide and facilitate $100bn of sustainable finance globally by 2025. HSBC UK has provided £0.7bn ($0.9bn) of green loans and sustainable finance to our customers in 2019 and £1.3bn ($1.7bn) since the 2017 announcement.

HSBC Group has issued $3.4bn of green and sustainability bonds. The HSBC Group green bond report provides a summary and the asset register lists the loans that underpin the issuances. The latest report include $1.1bn of balances as at 30 June 2019 that were booked on the HSBC UK balance sheet. The green bond and asset register is available at www.hsbc.com/investors/fixed-income-investors/green-and-sustainability-bonds.

Providing innovative green products — Derwent London plc case study

We have worked with our long standing customer Derwent London plc, a specialist property developer and investor with a design-led philosophy and a progressive and sustainable approach to development. We acted as "Green Loan Coordinator", "Mandated Lead Arranger" and coordinator to provide a £450m revolving credit facility. This facility included a £300m green tranche making it the first revolving credit facility provided to a real estate investment trust in the UK which is fully aligned to the LMA's GLP. The £300m Green tranche will be used to fund sustainable development and activities, all of which will be published in a report by Derwent and independently verified to ensure compliance with the GLP.

The Green tranche is available to fund activities that satisfy the criteria set out in Derwent's newly established 'Green Finance Framework'. This published document describes the group's sustainability objectives, specifies minimum 'Green' eligibility criteria and outlines how it intends to fund development and refurbishment projects that will deliver first class working, amenity and outdoor spaces, improved energy efficiency and reduced consumption of natural resources.

Supporting sustainable SMEs – e-cargobikes.com case study

e-cargobikes.com offer last-mile delivery services to grocers and retailers throughout the UK. e-cargobikes.com are an existing customer, who were looking for asset and invoice financing. They had already made significant commercial progress by securing a delivery contract from Co-op Food, and obtaining exclusive rights to their specific electric cargo-bike gave them an important competitive edge in the market. The e-cargo bike solution offers grocers and retailers an environmentally and financially sustainable alternative to fossil-fuelled vehicles in high-density urban areas. They also alleviate traffic congestion, create a safer community for all and promote active lifestyles.

The asset finance has the capacity to fund a further c.140 bikes to grow the fleet allowing the business to fulfil its obligations under the new contracts. HSBC UK were able to provide a holistic sustainable financing offering of a £0.5m asset purchasing facility, and a further £2m invoice finance facility to support e-cargobikes.com's fast growth.

e-cargobikes.com is just one example of how HSBC UK is supporting SMEs in the low carbon economy.

Retail Banking and Wealth Management

HSBC Global Sustainable Multi-Asset Portfolios are designed to provide capital growth through investment in assets that meet sustainable investment principles. We currently offer two risk-profiled portfolios – "Conservative" and "Balanced" – which offer global diversification with a higher Environmental, Social and Governance (ESG) score and a lower carbon intensity than the market.

Performance was strong over 2019 for both portfolios, with 9.96% growth in the Conservative portfolio and a 10.03% growth in the Balanced portfolio, over the one-year period from 30 November 2018 to 30 November 2019.

Given such strong demand and customer interest, we are aiming to launch three additional risk profile portfolios in the Global Sustainable Multi-Asset range ("Cautious", "Dynamic" and "Adventurous"). We are also intending to provide a Sustainable Model Portfolio Service for our internal and external discretionary customers across five risk profiles by the end of 2020.

Private Banking

In 2019, PB partnered with GB&M to offer its first green structured notes to customers. These structured notes finance green projects such as energy efficiency, renewable energy, waste and water treatment or public transportation. Customers have the advantage of tailoring the tenure, currency and underlying ESG index exposure to their investment needs while proceeds are being used for environmental purposes. These green structured notes are issued under the HSBC Green Bond framework, with a second party opinion from Cicero, a strategic advisory company.

Customers have the opportunity to follow up on the green projects they have helped finance through an annual report. This compliments our sustainable investment product range spanning across single line equity and fixed income, funds, exchange-traded funds and now structured notes.

Thought leadership, training, engagement

Thought leadership

We partnered with Imperial Business Partners and published a research paper called 'Lending to Low Carbon Technologies'. This reviewed the technology readiness levels for low-carbon solutions in the UK and presents a risk assessment from a bank lending perspective. The paper was written by researchers from Imperial College and is available on www.sustainablefinance.hsbc.com

Training

We continue to partner with Earthwatch, an environmental charity, to deliver our sustainability training programmes, which 132 colleagues attended in 2019.

In addition, 2,468 colleagues have completed online Sustainability training co-created with the University of Cambridge Institute for Sustainability Leadership.

Engagement

In 2019, we worked with WWF to highlight the ecological crisis and how it will impact businesses. We did this by promoting and screening their new film Our Planet: Our Business to our global network.

We also established a Climate Action Network in the UK led by passionate colleagues. These colleagues collaborate across all areas of the business to engage and educate our people on climate change and our sustainable operations strategy.

Sustainable operations

HSBC UK is committed to playing its part in supporting the transition to a low-carbon economy, both internally through our operations and externally by supporting our customers on their own transition journey.

Currently c.70% of our electricity comes from renewables through power purchase agreements for two wind farms and one solar farm. This helps move us closer to our ambition to source 100% of our electricity from renewable sources by 2030.

Reduce programme

As part of our Global Reduce Programme, we have committed to reduce CO2 emissions by 2 tonnes per full-time equivalent employee (FTE). By the end of 2019, globally we reached 2.26 tonnes and in the UK we have reached 1.08 tonnes per FTE.

Key Performance Indicators

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

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

Financial KPIs

Financial KPIs are included in the summary of Key Financial Metrics on page 2 and a review of these are detailed in the Financial Summary sections on pages 10 to 15 and the Capital section on pages 52 to 54.

Non-financial KPIs

We also monitor a range of non-financial KPIs focusing on our strategic priorities of customer experience, colleague engagement, shareholder value growth and simplification, as well as internal risk metrics. For in depth details on customer service and satisfaction please refer below; for diversity, inclusion and colleagues development, please refer to the corporate governance report on pages 54 to 59.

Customer service and satisfaction

We track our customer service and satisfaction through a series of industry measures across RBWM, CMB and PB.

Retail Banking and Wealth Management

In addition to the CMA rankings, we also use the Customer Recommendation Index (CRI), which measures customers' likelihood to recommend HSBC UK products and services to friends or family (scores out of 100). This measure is tracked relative to competitors.

Scores for HSBC UK RBWM have remained consistent since the end of 2018, with the overall score remaining at 76 in December 2019. In the CMA Service Quality Indicators, HSBC UK was ranked joint sixth in the February 2020 publication for overall service quality, with a score of 61%. This was an improvement of four percentage points and six ranking positions compared to the February 2019 release.

first direct continues to be a market leader for customer recommendation, and in February 2020 was ranked first in the CMA rankings. first direct also lead the market in CRI, ending the year with a score of 92, a one-point decline vs. 2018.

M&S Bank's CRI score has seen improvements across 2019, improving two points since December 2018, with a score of 78 in December 2019.

Commercial Banking

CMB has seen continued progress in the satisfaction of its customers, as measured by Savanta, reaching overall second position with all customer segments in the top three.

We continue to support our customers aspirations to grow their businesses both domestically and internationally, reflected by the strong perceptions of our lending support, where we are ranked joint third of twelve banks amongst SMEs (as measured within the February 2020 CMA Service Quality Indicator Study). CMB continues to be ranked the number one bank in the Savanta Survey for being able to support UK businesses trading internationally. Our international trade credentials were further endorsed with HSBC being named the market leader in global trade finance for the third year running in Euromoney magazine's Trade Finance Survey 2019.

Private Banking

In our annual internal Private Banking relationship survey we have seen a good year on year performance, with the UK satisfaction score increasing from a mean score of 7.8 out of 10 in 2018 to 8.1 in 2019. The improvements reflect a continued strength in the relationship with our customers, with customers' satisfaction with relationship management teams scoring 8.8, along with the supporting teams scoring 8.6.

Financial summary

The business and subsidiaries were in operation in HSBC Bank plc prior to the transfer to the bank on 1 July 2018. To provide better comparative information, the income statement is also presented for the six months 30 June 2019 ('1H19') and 31 December 2019 ('2H19').

Summary consolidated income statement for the year ended

	Year ended		Half-year to	
	Audited		Unaudited	
	31 Dec 2019	31 Dec 2018	**31 Dec 2019**	30 Jun 2019
	£m	£m	**£m**	£m
Net interest income	**4,752**	2,456	**2,315**	2,437
Net fee income	**1,230**	648	**612**	618
Net income from financial instruments held for trading or managed on a fair value basis	**400**	198	**192**	208
Changes in fair value of other financial instruments mandatorily measured at fair value through profit or loss	**2**	–	**2**	–
Gains less losses from financial investments	**48**	22	**19**	29
Other operating income	**52**	33	**29**	23
Total operating income[1]	**6,484**	3,357	**3,169**	3,315
Net operating income before change in expected credit losses and other credit impairment charges ('Revenue')	**6,484**	3,357	**3,169**	3,315
Change in expected credit losses and other credit impairment charges	**(613)**	(305)	**(281)**	(332)
Net operating income	**5,871**	3,052	**2,888**	2,983
Total operating expenses[1]	**(4,861)**	(1,988)	**(2,494)**	(2,367)
Operating profit	**1,010**	1,064	**394**	616
Profit before tax	**1,010**	1,064	**394**	616
Tax expense	**(494)**	(301)	**(229)**	(265)
Profit for the year	**516**	763	**165**	351
Profit attributable to shareholders of the parent company	**512**	763	**164**	348
Profit attributable to non-controlling interests	**4**	–	**1**	3

1 Total operating income and expenses includes significant items as detailed on pages 12 to 14.

Reported performance

2019 Full Year ('FY') reported profit before tax was £1,010m. 2H19 reported profit before tax of £394m was £222m, 36%, lower than 1H19 and £670m, 63%, lower than six months 31 December 2018 ('2H18'), both driven by the negative impact of significant items in both revenue and operating expenses.

2019 FY **Net interest income ('NII')** was £4,752m. 2H19 NII of £2,315m was £122m, 5%, lower than 1H19 and £141m, 6%, lower than 2H18, both due to increased customer redress programme provisions.

2019 FY **Net fee income ('NFI')** was £1,230m. 2H19 NFI of £612m was £6m, 1% lower than 1H19. 2H19 NFI was £36m, 6%, lower than 2H18 due to additional CMB customer redress provisions.

2019 FY **Net income from financial instruments held for trading or managed on a fair value basis** was £400m and £192m in 2H19, which was £16m, 8%, lower than 1H19 , driven by seasonal factors in the GB&M foreign currency exchange revenue. 2H19 was £6m, 3%, lower than 2H18.

2019 FY **Gains less losses from financial investments** were £48m and £19m in 2H19, which were £10m, 34%, lower than 1H19 driven from lower disposal gains and losses taken when reducing risk during the heightened geopolitical risk in 4Q19 in the Balance Sheet Management function. 2H19 was £3m, 14%, lower than 2H18.

2019 FY **Other operating income** was £52m. 2H19 other operating income of £29m was £6m, 26%, higher than 1H19 and £4m,12%, lower than 2H18.

2019 FY **Expected credit losses and other credit impairment charges ('ECL')** were £613m. 2H19 ECL of £281m were £51m, 15%, lower than 1H19 and £24m, 8%, lower than 2H18, both largely driven by changes in allowances for UK economic uncertainty.

2019 FY **Operating expenses** were £4,861m. 2H19 operating expenses of £2,494m were £127m, 5% higher than 1H19. 2H19 were £506m, 25% higher than 2H18 driven by a number of significant items including:

- Higher UK customer redress provisions of £490m.
- An increase of £52m in restructuring and other related costs.

Offset by:

- Pension costs of £187m in 2H18 following the October 2018 High Court judgement on Guaranteed Minimum Pension equalisation ('GMP').

Excluding significant items, 2H19 operating expenses were £144m higher than 2H18 mainly due to additional customer redress provisions (not classified as significant items) and increases in fraud, investment and regulatory costs.

For further details of significant items affecting revenue and costs, please refer to significant revenue/cost items by business segment on pages 12 to 14.

Net interest income

	Year ended	
	31 Dec 2019	31 Dec 2018
	£m	£m
Interest income	**5,696**	2,805
Interest expense	**(944)**	(349)
Net interest income	**4,752**	2,456
Average interest-earning assets	**231,701**	219,419
	%	%
Gross interest yield[1]	**2.46**	2.53
Less: cost of funds	**(0.53)**	(0.37)
Net interest spread[2]	**1.93**	2.16
Net interest margin[3, 4]	**2.05**	2.22

1 Gross interest yield is the average annualised interest rate earned on average interest-earning assets ('AIEA').
2 Net interest spread is the difference between the average annualised interest rate earned on AIEA, net of amortised premiums and loan fees, and the average annualised interest rate payable on average interest-bearing funds.
3 Net interest margin is net interest income expressed as an annualised percentage of AIEA.
4 Net interest margin of 2.05% includes a reduction of 5bps (2018: 0bps) due to significant items.

Net interest margin ("NIM") decreased from 2.22% in 2H18 to 2.05% in 2019. This is driven by customer redress provisions impacting NII, an increase in cost of funds, due to the issuance of debt securities and subordinated debt in 2019, and a shift in the loan mix towards retail mortgages.

Return on average tangible equity ('RoTE') (%)

ROTE (%) is measured as the profit attributable to the ordinary shareholders divided by the reported equity adjusted for goodwill and intangibles. The 2019 RoTE of 2.4% was 6.4% lower than the 2H18 (annualised) RoTE of 8.8% driven by lower Reported profit before tax.

Non-GAAP financial measures

Our reported results are prepared in accordance with IFRSs, as detailed in the financial statements starting on page 70. In measuring our performance, the financial measures that we use include those derived from our reported results in order to eliminate factors that distort year-on-year comparisons. These are considered non-GAAP financial measures.

Within the Strategic Report we present performance on an adjusted basis, which is our segment measure for our reportable segments under IFRS 8 but constitutes a non-GAAP financial measure when otherwise presented.

Adjusted performance

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

We use significant items to describe collectively the group of individual adjustments excluded from the results when arriving at adjusted performance. An item might be deemed significant if the item is not incurred as part of the normal operational activities of the individual segment, separate identification and explanation of the item is necessary in order for users to gain a proper understanding of the performance of the business, and it is quantitatively and qualitatively material to the Group's consolidated financial statements. Customer remediation and redress programmes, which constitute the majority of the group's significant items, are considered and assessed separately against the above criteria prior to recognition as a significant item.

Significant items, which are detailed on pages 12 to 14, are ones that management and investors would ordinarily identify and consider separately when assessing performance to understand better the underlying trends in the business. We consider adjusted performance to provide useful information for investors by aligning internal and external reporting, identifying and quantifying items management believes to be significant and providing insight into how management assesses year-on-year performance.

Segmental reporting

Global businesses are our reportable segments under IFRS 8.

The HSBC Group Chief Executive, supported by the rest of the Group Management Board, is considered the Chief Operating Decision Maker for the purposes of identifying the HSBC Group's, and therefore HSBC UK's, reportable segments. HSBC UK's chief operating decision-maker is the HSBC UK Chief Executive, supported by the HSBC UK Executive Committee. The global business results are assessed by the HSBC UK Chief Operating Decision Maker on the basis of adjusted performance that removes the effects of significant items from results. We therefore present HSBC UK global business results on an adjusted basis.

Our operations are closely integrated and, accordingly, the presentation of data includes internal allocations of certain items of income and expense. These allocations include the costs of certain support services and global functions to the extent that they can be meaningfully attributed to operational business lines. While such allocations have been made on a systematic and consistent basis, they necessarily involve a degree of subjectivity. Costs which are not allocated to global businesses are included in Corporate Centre. Where relevant, income and expense amounts presented include the results of inter-segment funding along with inter-company and inter-business line transactions. All such transactions are undertaken on arm's length terms. The intra-group elimination items are presented in the Corporate Centre.

A description of the global businesses is provided in the Strategic Report, page 3.

Adjusted profit before tax and balance sheet data for the year ended (audited)

31 Dec 2019	RBWM £m	CMB £m	GB&M £m	PB £m	Corporate Centre £m	Total £m
Net operating income before change in expected credit losses and other credit impairment charges	3,488	2,708	176	158	83	6,613
– external	3,466	2,716	173	158	100	6,613
– inter-segment	22	(8)	3	–	(17)	–
of which; net interest income	*2,775*	*1,951*	*1*	*106*	*45*	*4,878*
Change in expected credit losses and other credit impairment charges	(295)	(299)	–	(19)	–	(613)
Net operating income	3,193	2,409	176	139	83	6,000
Total operating (expenses)/income	(2,339)	(1,209)	(122)	(125)	58	(3,737)
Operating profit	854	1,200	54	14	141	2,263
Adjusted profit before tax	854	1,200	54	14	141	2,263
	%	%	%	%	%	%
Adjusted cost efficiency ratio	67.1	44.6	69.3	79.1	(69.9)	56.5
Balance sheet information	£m	£m	£m	£m	£m	£m
Loans and advances to customers (net)	113,732	64,772	–	4,293	259	183,056
Customer accounts	134,737	75,758	–	5,921	(202)	216,214

Adjusted profit before tax and balance sheet data for the year ended (audited) (continued)

31 Dec 2018	RBWM £m	CMB £m	GB&M £m	PB £m	Corporate Centre £m	Total £m
Net operating income before change in expected credit losses and other credit impairment charges	1,766	1,378	72	78	58	3,352
– external	1,747	1,365	74	78	88	3,352
– inter-segment	19	13	(2)	–	(30)	–
of which: net interest income/(expense)	*1,391*	*979*	*(3)*	*57*	*28*	*2,452*
Change in expected credit losses and other credit impairment charges	(164)	(145)	–	4	–	(305)
Net operating income	1,602	1,233	72	82	58	3,047
Total operating (expenses)/income	(1,125)	(530)	(69)	(54)	30	(1,748)
Operating profit	477	703	3	28	88	1,299
Adjusted profit before tax	477	703	3	28	88	1,299
	%	%	%	%	%	%
Adjusted cost efficiency ratio	63.7	38.5	95.8	69.2	(51.7)	52.1
Balance sheet information	£m	£m	£m	£m	£m	£m
Loans and advances to customers (net)	106,609	63,302	–	4,269	627	174,807
Customer accounts	128,409	71,411	–	5,338	(321)	204,837

Adjusted profit before tax for the half year ended

31 Dec 2019	RBWM £m	CMB £m	GB&M £m	PB £m	Corporate Centre £m	Total £m
Net operating income before change in expected credit losses and other credit impairment charges	**1,771**	**1,331**	**87**	**81**	**28**	**3,298**
– external	**1,755**	**1,341**	**87**	**81**	**34**	**3,298**
– inter-segment	**16**	**(10)**	**–**	**–**	**(6)**	**–**
of which: net interest income/(expense)	***1,406***	***961***	***(1)***	***53***	***22***	***2,441***
Change in expected credit losses and other credit impairment charges	**(159)**	**(119)**	**–**	**(3)**	**–**	**(281)**
Net operating income	**1,612**	**1,212**	**87**	**78**	**28**	**3,017**
Total operating (expenses)/income	**(1,173)**	**(647)**	**(59)**	**(64)**	**51**	**(1,892)**
Operating profit	**439**	**565**	**28**	**14**	**79**	**1,125**
Adjusted profit before tax	**439**	**565**	**28**	**14**	**79**	**1,125**
	%	**%**	**%**	**%**	**%**	**%**
Adjusted cost efficiency ratio	**66.2**	**48.8**	**67.8**	**79.0**	**(182.1)**	**57.4**

30 Jun 2019						
Net operating income before change in expected credit losses and other credit impairment charges	1,717	1,377	89	77	55	3,315
– external	1,711	1,375	86	77	66	3,315
– inter-segment	6	2	3	–	(11)	–
of which: net interest income	*1,369*	*990*	*2*	*53*	*23*	*2,437*
Change in expected credit losses and other credit impairment charges	(136)	(180)	–	(16)	–	(332)
Net operating income	1,581	1,197	89	61	55	2,983
Total operating (expenses)/income	(1,166)	(562)	(63)	(61)	7	(1,845)
Operating profit	415	635	26	–	62	1,138
Adjusted profit before tax	415	635	26	–	62	1,138
	%	%	%	%	%	%
Adjusted cost efficiency ratio	67.9	40.8	70.8	79.2	(12.7)	55.7

Significant revenue items by business segment – (gains)/losses for the year ended (audited)

31 Dec 2019	RBWM £m	CMB £m	GB&M £m	PB £m	Corporate Centre £m	Total £m
Revenue	**3,364**	**2,703**	**176**	**158**	**83**	**6,484**
Significant revenue items	**124**	**5**	**–**	**–**	**–**	**129**
– customer redress programmes	**124**	**5**	**–**	**–**	**–**	**129**
Adjusted revenue	**3,488**	**2,708**	**176**	**158**	**83**	**6,613**

31 Dec 2018						
Revenue	1,766	1,383	72	78	58	3,357
Significant revenue items	–	(5)	–	–	–	(5)
– customer redress programmes	–	(5)	–	–	–	(5)
Adjusted revenue	1,766	1,378	72	78	58	3,352

Significant revenue items by business segment – (gains)/losses for the half year ended

31 Dec 2019	RBWM £m	CMB £m	GB&M £m	PB £m	Corporate Centre £m	Total £m
Revenue	1,647	1,326	87	81	28	3,169
Significant revenue items	124	5	–	–	–	129
– customer redress programmes	124	5	–	–	–	129
Adjusted revenue	1,771	1,331	87	81	28	3,298
30 Jun 2019						
Revenue	1,717	1,377	89	77	55	3,315
Significant revenue items	–	–	–	–	–	–
Adjusted revenue	1,717	1,377	89	77	55	3,315

Significant cost items by business segment for the year ended (audited)

31 Dec 2019	RBWM £m	CMB £m	GB&M £m	PB £m	Corporate Centre £m	Total £m
Operating expenses	(3,393)	(1,234)	(122)	(127)	15	(4,861)
Significant cost items	1,054	25	–	2	43	1,124
– restructuring and other related costs[1]	55	11	–	2	43	111
– customer redress programmes	999	14	–	–	–	1,013
Adjusted operating expenses	(2,339)	(1,209)	(122)	(125)	58	(3,737)
31 Dec 2018						
Operating expenses	(1,186)	(518)	(69)	(54)	(161)	(1,988)
Significant cost items	61	(12)	–	–	191	240
– costs of structural reform	1	2	–	–	11	14
– customer redress programmes	60	(14)	–	–	–	46
– guaranteed minimum pension benefits equalisation	–	–	–	–	187	187
– other	–	–	–	–	(7)	(7)
Adjusted operating expenses	(1,125)	(530)	(69)	(54)	30	(1,748)

Significant cost items by business segment for the half year ended

31 Dec 2019	RBWM £m	CMB £m	GB&M £m	PB £m	Corporate Centre £m	Total £m
Operating expenses	(1,728)	(663)	(59)	(66)	22	(2,494)
Significant cost items	555	16	–	2	29	602
– restructuring and other related costs[1]	34	2	–	2	29	67
– customer redress programmes	521	14	–	–	–	535
Adjusted operating expenses	(1,173)	(647)	(59)	(64)	51	(1,892)
30 Jun 2019						
Operating expenses	(1,665)	(571)	(63)	(61)	(7)	(2,367)
Significant cost items	499	9	–	–	14	522
– restructuring and other related costs[1]	21	9	–	–	14	44
– customer redress programmes	478	–	–	–	–	478
Adjusted operating expenses	(1,166)	(562)	(63)	(61)	7	(1,845)

1 *Restructuring costs include charges received from HSBC Global Services (UK) Limited, which do not form part of the balance sheet provision movement.*

Net impact on profit before tax by business segment for the year ended (audited)

31 Dec 2019	RBWM £m	CMB £m	GB&M £m	PB £m	Corporate Centre £m	Total £m
Profit/(loss) before tax	(324)	1,170	54	12	98	1,010
Net Impact on reported profit and loss	1,178	30	–	2	43	1,253
– significant revenue items	124	5	–	–	–	129
– significant cost items	1,054	25	–	2	43	1,124
Adjusted profit before tax	854	1,200	54	14	141	2,263
31 Dec 2018						
Profit/(loss) before tax	416	720	3	28	(103)	1,064
Net Impact on reported profit and loss	61	(17)	–	–	191	235
– significant revenue items	–	(5)	–	–	–	(5)
– significant cost items	61	(12)	–	–	191	240
Adjusted profit before tax	477	703	3	28	88	1,299

Net impact on profit before tax by business segment for the half year ended

31 Dec 2019	RBWM £m	CMB £m	GB&M £m	PB £m	Corporate Centre £m	Total £m
Profit/(loss) before tax	(240)	544	28	12	50	394
Net Impact on reported profit and loss	679	21	–	2	29	731
– significant revenue items	124	5	–	–	–	129
– significant cost items	555	16	–	2	29	602
Adjusted profit before tax	439	565	28	14	79	1,125
30 Jun 2019						
Profit/(loss) before tax	(84)	626	26	–	48	616
Net Impact on reported profit and loss	499	9	–	–	14	522
– significant revenue items	–	–	–	–	–	–
– significant cost items	499	9	–	–	14	522
Adjusted profit before tax	415	635	26	–	62	1,138

Adjusted performance

Our 2019 adjusted profit before tax was £2,263m. 2H19 adjusted profit before tax of £1,125m was £13m, 1%, lower than 1H19 and £174m, 13%, lower than 2H18. These variances reflect higher adjusted operating expenses and lower adjusted revenue offset by lower expected credit losses and other credit impairment charges ('ECL').

2019 FY adjusted revenue was £6,613m. 2H19 adjusted revenue of £3,298m was £17m, 1%, lower than 1H19. 2H19 adjusted revenue was £54m, 2% lower than 2H18 driven by additional customer redress provisions not classified as significant items in CMB.

2019 FY ECL were £613m. 2H19 ECL of £281m were £51m, 15%, lower than 1H19 and £24m, 8%, lower than 2H18, both largely driven by changes in allowances for UK economic uncertainty.

2019 FY adjusted operating expenses were £3,737m. 2H19 adjusted operating expense of £1,892m were £47m, 3%, higher than 1H19 and £144m, 8%, higher than 2H18, increases driven by additional customer redress provisions not classified as significant items, and increases in fraud, investment and regulatory costs.

The 2019 adjusted RoTE of 9.9% was 1.8% lower than the 2H18 (annualised) adjusted RoTE of 11.7% driven by lower adjusted profit before tax.

Adjusted cost efficiency ratio is measured as total adjusted operating expenses divided by adjusted net operating income before ECL. The adjusted cost efficiency ratio in 2019 increased by 4.4% vs. 2018, from 52.1% to 56.5%.

Retail Banking and Wealth Management

2019 FY adjusted profit before tax was £854m, 2H19 was £439m, £24m, 6%, higher than 1H19 driven by higher revenue partially offset by higher ECL. 2H19 compared to 2H18 is £38m, 8%, lower primarily driven from higher operating expenses.

2019 FY adjusted revenue was £3,488m, 2H19 was £1,771m, £54m, 3%, higher than 1H19 driven from balance growth in mortgages, loans and current accounts. 2H19 revenue was £5m higher than 2H18.

2019 FY ECL were £295m. 2H19 ECL of £159m were £23m, 17%, higher than 1H19, driven by portfolio growth and model updates partly offset by a release of allowances related to economic uncertainty. 2H19 ECL were £5m, 3%, lower than 2H18.

2019 FY adjusted operating expenses were £2,339m, 2H19 were £1,173m, £7m, 1%, higher than 1H19. 2H19 were £48m, 4%, higher than 2H18 due to increased fraud costs, additional customer redress provisions, increased investment costs and wage inflation.

Commercial Banking

2019 FY adjusted profit before tax was £1,200m. 2H19 adjusted profit before tax of £565m was £70m, 11%, lower than 1H19 and £138m, 20%, lower than 2H18 both due to lower revenue and higher operating expenses offset by lower ECL.

2019 FY adjusted revenue was £2,708m, 2H19 was £1,331m, £46m, 3%, lower than 1H19 and £47m, 3%, lower than 2H18. The revenue reduction in 2H19 reflects additional customer redress provisions.

2019 FY ECL were £299m. 2H19 ECL of £119m were £61m, 34%, lower than 1H19 and £26m, 18%, lower than 2H18. The decrease in 2H19 ECL has largely been driven by changes in allowances for UK economic uncertainty.

2019 FY adjusted operating expenses were £1,209m, 2H19 were £647m, £85m, 15%, higher than 1H19 and £117m, 22%, higher than 2H18, the increases have been driven by additional customer redress provisions, increases in fraud and regulatory costs.

Global Banking and Markets

GB&M in HSBC UK reflects the transacting of foreign currency exchange for RBWM and CMB customers. The majority of the foreign exchange revenue is passed over to RBWM and CMB, with an element retained in GB&M.

2019 FY adjusted profit before tax was £54m, 2H19 was £28m, £2m, 7%, higher than 1H19. 2H19 was £25m higher than 2H18 due to higher revenue and lower operating expenses.

2019 FY adjusted revenue was £176m, 2H19 was £87m, in line with 1H19 revenue of £89m. 2H19 was £15m, 21%, higher than 2H18 due to increases in revenue share agreements and favourable market conditions driving increasing foreign exchange revenues.

2019 FY adjusted operating expenses were £122m, 2H19 adjusted operating expenses of £59m were £4m, 6%, lower than 1H19 and £10m, 14%, lower than 2H18 both due to lower costs of back and middle office foreign exchange activities.

Private Banking

2019 FY adjusted profit before tax was £14m. 2H19 adjusted profit was £14m, £14m higher than 1H19 due lower ECL. 2H19 was £14m, 50%, lower than 2H18 driven by higher operating expenses.

2019 FY adjusted revenue was £158m, 2H19 was £81m, £4m, 5%, higher than 1H19 and £3m, 4%, higher than 2H18 driven by higher annuity fee and investment product income.

2019 ECL were £19m, 2H19 were £3m, £13m, 81%, lower than 1H19 due to lower impairments and default rates. 2H19 ECL were £7m higher than 2H18 due to a net recovery position in 2H18.

2019 FY adjusted operating expenses were £125m. 2H19 adjusted operating expenses of £64m were £3m, 5%, higher than 1H19. 2H19 were £10m, 19%, higher than 2H18 driven by increases in technology, operations and legal costs.

Corporate Centre

2019 FY adjusted profit before tax was £141m. 2H19 adjusted profit before tax of £77m was £17m, 27%, higher than 1H19 and £10m, 11%, lower than 2H18.

2019 FY adjusted revenue was £83m. 2H19 adjusted revenue of £28m was £27m, 49%, lower than 1H19 and £30m, 52%, lower

than 2H18 driven by lower disposal gains and losses taken when reducing risk during the heightened geopolitical risk in 4Q19 in the Balance Sheet Management function, and issuance fees and fair value volatility on subordinated liabilities incurred in 2H19.

2019 FY adjusted operating expenses were a net income of £58m, driven by income from the IAS19 pension surplus. 2H19 adjusted operating expenses net income of £51m was £44m higher than 1H19, due to reduced support costs and a higher net income from the IAS 19 pension surplus. 2H19 net income was £21m higher than 2H18 due to a higher net income from the IAS 19 pension surplus.

Dividends

The consolidated reported profit for the year attributable to the shareholders of the bank was £512m. Interim dividends of £200m, in lieu of a final dividend in respect of the previous financial year, and £120m in respect of 2019 were paid on the ordinary share capital during the year.

An interim dividend of £100m, in lieu of a final dividend in respect of the current year, was declared after 31 December 2019, payable on 19 March 2020.

Further information regarding dividends is given in Note 6.

Summary consolidated balance sheet as at

	31 Dec 2019 £m	31 Dec 2018 £m
Total assets	**257,102**	238,939
– cash and balances at central banks	**37,030**	33,193
– items in the course of collections from other banks	**504**	603
– financial assets designated and otherwise mandatory measured at fair value	**66**	35
– derivative assets	**121**	66
– loans and advances to banks	**1,389**	1,263
– loans and advances to customers	**183,056**	174,807
– reverse repurchase agreements – non trading	**3,014**	3,422
– financial investments	**19,737**	13,203
– prepayment, accrued income and other assets	**8,212**	8,537
– goodwill and intangible assets	**3,973**	3,810
Total liabilities	**234,851**	216,606
– deposits by banks	**529**	1,027
– customer accounts	**216,214**	204,837
– repurchase agreements – non trading	**98**	639
– *items in the course of transmission to other banks*	**343**	233
– derivative liabilities	**201**	346
– debt securities in issue	**3,142**	–
– accruals, deferred income and other liabilities	**1,834**	2,409
– current and deferred tax liabilities	**1,632**	1,548
– provisions	**1,325**	630
– subordinated liabilities	**9,533**	4,937
Total equity	**22,251**	22,333
– total shareholders' equity[1]	**22,191**	22,273
– non-controlling interests	**60**	60

1 *Total shareholders' equity includes share capital, share premium, additional Tier 1 instruments and reserves. Reserves include accounting reserves relating to the recognition of goodwill and the pension asset net of deferred tax which do not form part of regulatory capital.*

The group maintained a strong and liquid balance sheet. The ratio of customer advances to customer accounts decreased slightly to 84.7% compared to 85.3% at 31 December 2018.

Assets

Cash and balances at central banks increased by 12%, and financial investments increased by 49%, as we continued to manage our liquid assets.

Loans and advances to customers increased by 5% due to growth in retail and commercial lending, particularly in retail mortgages.

Liabilities

Customer accounts increased by 6% due to growth in commercial and retail balances.

Subordinated liabilities increased by 93% due to debt issued to HSBC Holdings plc for Minimum Requirements for own funds and Eligible Liabilities ('MREL') compliance.

Debt securities in issue has increased as HSBC UK issued senior unsecured debt for funding and liquidity purposes, and securities for credit risk mitigation purposes.

Equity

Total shareholders' equity remained in line with that at 31 December 2018.

Risk overview

We continuously identify and monitor risks. This process, which is informed by our risk factors and the results of the stress testing programme, gives rise to the classification of certain principal risks. Changes in the assessment of principal risks may result in adjustments to our business strategy and, potentially, our risk appetite.

Our banking risks include credit risk, capital and liquidity risk, market risk, resilience risk, regulatory compliance risk, financial crime and fraud risk and model risk.

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

The exposure to our risks and risk management of these are explained in more detail in the Risk section of the Report of the Directors on pages 17 to 51.

During 2019, a number of changes to our top and emerging risks have been made, to reflect the revised assessment of their effect on HSBC UK.

Two risks have been added in 2019. These are 'Climate-related risks' and 'Third party risk management'.

Risk		Mitigants
Externally driven		
Geopolitical risk	▶	We continually assess the impact of geopolitical events on our businesses and exposures across HSBC UK, and take steps to mitigate them, where required and possible, to help ensure we remain within our risk appetite. The UK left the EU on 31 January 2020. We will continue to work with regulators, governments and our customers to manage the risks created by the UK's exit from the EU as they arise, particularly across those industry sectors most impacted.
Turning of the credit cycle	▲	We continue to undertake detailed reviews of our portfolios and are also proactively assessing customers and industry sectors likely to come under stress as a result of geopolitical or macroeconomic events, reducing limits where appropriate.
Regulatory developments	▶	We proactively engage with regulators and policy makers, wherever possible, to help ensure that new regulatory requirements are considered fully and can be implemented in an effective manner.
Information security risk and cyber crime	▶	We continue to strengthen our cyber control framework and improve our resilience and cybersecurity capabilities, including threat detection and analysis, access control, payment system controls, data protection, network controls and backup and recovery.
Ibor transition	▲	HSBC UK is part of the HSBC Group Interbank Offered Rates ('Ibor') transition programme. This programme is focussed on replacing Ibors by developing processes and systems to support alternative rate products and making these available to our clients. The programme is developing the proposed transition operating model to re-paper outstanding Libor and Eonia contracts. We have identified a number of potential execution, conduct and financial risks and are in the process of addressing these. We continue to engage with industry bodies, regulators and our clients to support an orderly transition.
Climate-related risks	●	The HSBC Group are committed to facilitating the re-allocation of capital to help finance the global transition to a low- carbon economy. The Group continues to make progress in this area. We regularly review our sustainability risk policies to ensure they remain fit-for-purpose, while still supporting customers. We have initiated the analysis of the impact of transition risk on our credit portfolio.
Internally driven		
People risk	▶	We continue to monitor workforce capacity and capability requirements in line with our strategy and any emerging issues in the UK market. These issues can include changes to immigration and tax rules as well as industry-wide regulatory changes.
IT systems infrastructure and resilience	▶	We actively monitor and improve service resilience across our technology infrastructure. We are enhancing the end-to-end mapping of key processes, and strengthening our problem diagnosis/resolution and change execution capabilities, seeking to reduce service disruption to our customers.
Execution risk	▶	We continue to strengthen our prioritisation and governance processes for significant strategic, regulatory and compliance projects.
Model risk	▲	We have evolved our model risk management capability and practice by enhancing the second line of defence Model Risk Management function, strengthening model oversight, and by evolving our model risk governance framework.
Conduct and customer detriment	▲	We continue to enhance our management of conduct in a number of areas, including the treatment of potentially vulnerable customers, governance of product arrangements, and encouragement of a 'Speak Up' culture.
Financial crime and fraud risk	▶	Throughout 2019, we continued to implement the final elements of the Global Standards programme to integrate our anti-money laundering and sanctions capabilities into our day-to-day operations. We continue to enhance our financial crime risk management capabilities and the effectiveness of our financial crime controls, with investment being maintained in the next generation of tools to fight financial crime through the application of advanced analytics and artificial intelligence.
Data management	▶	We continue to enhance and advance our data insights, data aggregation, reporting and decisions through ongoing improvement and investments in data governance, data quality, data privacy, data architecture, machine learning and artificial intelligence capabilities.
Third party risk management	●	We continue to strengthen essential governance processes and relevant policies relating to how we identify, assess, mitigate and manage risks across the range of third parties with which we do business. This includes control monitoring and assurance throughout the third-party life cycle.

▲ Risk has heightened during 2019

▶ Risk remains at the same level as 2018

● New Risk introduced during 2019

The Strategic Report comprising pages 2 to 16 was approved by the Board on 17 February 2020 and is signed on its behalf by

John David Stuart
Director
HSBC UK Bank plc
Registered number: 9928412

Risk

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Our conservative risk appetite

We maintain a conservative risk profile. This is central to our business and strategy.

We recognise that the primary role of risk management is to protect our business, customers, colleagues, shareholders and the communities that we serve whilst supporting our strategy and enabling sustainable growth.

We recognise the importance of a strong risk culture, which refers to our shared attitudes, values and norms that shape behaviours related to risk awareness, risk taking and risk management. All employees are responsible for the management of risk, with the ultimate responsibility residing with the Board.

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

Financial position

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

Operating model

- Generate returns in line with a conservative risk appetite and strong risk management capability.
- Deliver sustainable earnings and consistent returns for shareholders.

Business practice

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

Enterprise-wide application

Our risk appetite encapsulates consideration of financial and non-financial risks and is expressed in both quantitative and qualitative terms. It applies across all our business lines.

Our risk management framework

An established risk governance framework and ownership structure ensures oversight of, and accountability for, the effective management of risk. Our Enterprise Risk Management Framework ('ERMF') fosters the continuous monitoring of the risk environment and an integrated evaluation of risks and their interactions. Integral to our risk management framework are risk appetite, stress testing and the identification of emerging risks.

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

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

Responsibility for managing both financial and non-financial risk lies with our people. They are required to manage the risks of the business and operational activities for which they are responsible. We maintain oversight of our risks through our various specialist Risk Stewards, as well as the accountability held by the Chief Risk Officer.

Non-financial risk includes some of the most material risks HSBC UK faces, such as cyber attacks, the loss of data and poor conduct outcomes. Actively managing non-financial risk is crucial to serving our customers effectively and having a positive impact on society. During 2019, we continued to strengthen the control environment and our approach to the management of non-financial risk, as set out in our Operational Risk Management Framework ('ORMF'). The approach outlines non-financial risk governance and risk appetite, and provides a single view of the key non-financial risks, and associated controls. It incorporates a risk management system designed to enable the active management of non-financial risk. Our ongoing focus is on simplifying our approach to non-financial risk management, while driving more effective oversight and better end-to-end identification and management of non-financial risks. This is overseen by the Operational Risk Management function, headed by the HSBC UK Head of Operational Risk.

Three lines of defence

To create a robust control environment to manage risks, we use an activity-based three lines of defence model. This model delineates management accountabilities and responsibilities for risk management and the control environment.

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

- The first line of defence owns the risks and is responsible for identifying, recording, reporting and managing them in line with risk appetite, and ensuring that the right controls and assessments are in place to mitigate them.
- The second line of defence challenges the first line of defence on effective risk management, and provides advice and guidance in relation to the risk.
- The third line of defence is our Global Internal Audit function, which provides independent assurance that our risk management approach and processes are designed and operating effectively.

Our risk culture

Our risk culture is reinforced by our values. It is instrumental in aligning the behaviours of individuals with our attitude to assuming and managing risk, which helps to ensure that our risk profile remains in line with our risk appetite.

We use clear and consistent employee communication on risk to convey strategic messages and set the tone from senior management and our Board. We also deploy mandatory training

on risk and compliance topics to embed skills and understanding in order to strengthen our risk culture and reinforce the attitude to risk in the behaviour expected of employees, as described in our risk policies.

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

Whistleblowing

The Group operate a whistleblower platform, HSBC Confidential, allowing staff to report matters of concern confidentially that, where necessary, are escalated to the Board. The Group also maintain an external email address for concerns about accounting and internal financial controls or auditing matters (accountingdisclosures@hsbc.com).

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

Risk appetite

We formally articulate our risk appetite through our risk appetite statement ('RAS'), which is approved by the Board on the recommendation of the Risk Committee. Setting out our risk appetite ensures that planned business activities provide an appropriate balance of return for the risk we are taking, and that we agree a suitable level of risk for our strategy. In this way, risk appetite informs our financial planning process and helps senior management to allocate capital to business activities, services and products.

The RAS consists of qualitative statements and quantitative metrics, covering financial and non-financial risks. It is fundamental to the development of business line strategies, strategic and business planning and senior management balanced scorecards. Performance against the RAS is reported to the Risk Management Meeting ('RMM') on a monthly basis so that any actual performance that falls outside the approved risk appetite is discussed and appropriate mitigating actions are determined. This reporting allows risks to be promptly identified and mitigated, and informs risk-adjusted remuneration to drive a strong risk culture.

Our RAS and business activities are guided and underpinned by qualitative principles and/or quantitative metrics.

Risk management

As a provider of banking and financial services, we actively manage risk as a core part of our day-to-day activities. We continue to maintain a strong liquidity position and are well positioned for the evolving regulatory landscape. We also maintained our conservative risk profile in 2019.

Stress testing

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

A number of internal macroeconomic and event-driven scenarios specific to the UK or the global economy were considered and reported to senior management during the course of the year. These scenarios included considering highly adverse outcomes in relation to the UK's withdrawal from the EU. HSBC UK also conducted Reverse Stress Testing. This exercise required HSBC UK to assess scenarios and circumstances that would render its business model non-viable, thereby identifying potential business vulnerabilities.

Furthermore, HSBC UK is subject to regulatory stress testing and the requirements are increasing in frequency and granularity. The assessment by the regulators is on both a quantitative and qualitative basis, the latter focusing on our portfolio quality, data provision, stress testing capability and capital planning processes.

In 2019, HSBC UK contributed to the successful completion of the HSBC Group's annual Bank of England ('BoE') concurrent stress testing exercise. The stresses applied to economic activity and financial market prices in the 2019 Annual Cyclical Scenario were the same as in the 2018 test. The scenario incorporates a severe and synchronised UK and global macro-economic and financial market stress, as well as an independent stress of misconduct costs. The Prudential Regulation Authority ('PRA') considered the scenario still appropriate in the context of prevailing domestic and global economic risks.

The BoE published the results of the 2019 Concurrent Stress Test in December 2019, confirming that these tests did not reveal any capital inadequacies for the HSBC Group. In 2020, HSBC UK will be submitting results to the PRA produced on a standalone basis.

Key developments and risk profile

Key developments in 2019

- We continued to strengthen our approach to managing non-financial risk, as set out in the ORMF. The framework sets out our approach to governance and risk appetite. It enables a single view of key non-financial risks and associated controls. This is overseen by the operational risk function, headed by HSBC UK's Head of Operational Risk. We also integrated our operational risk and conduct frameworks to better assess and mitigate conduct risks.
- The HSBC Group simplified its risk taxonomy used within HSBC UK through consolidating certain existing risks into broader categories, for example Resilience Risk. These changes streamline risk reporting and promote common language in our risk management approach. Further simplification will continue during 2020, including combining the HSBC Group's two key risk management frameworks, the ERMF and the ORMF, into one.
- We started the process to form a Resilience Risk sub-function to reflect the growing importance of operational resilience. The resilience risk sub function will be led from 1Q20 by a newly appointed HSBC UK Head of Resilience Risk.

Top and emerging risks

Top and emerging risks are those that may impact on our financial results, reputation or business model. If these risks were to occur, they could have a material effect on HSBC UK.

The exposure to these risks and our risk management approach are explained in more detail below.

Externally driven

Geopolitical risk

The UK left the EU on 31 January 2020, and entered a period of transition until 31 December 2020. We will continue to work with regulators, governments and our customers and employees to manage the risks resulting from the UK's exit from the EU as they arise, particularly across those industry sectors most impacted.

A conclusive outcome to the general election in December 2019 has improved the UK's political stability. However, uncertainty regarding the terms of the UK's future relationship (including trading) with both the EU and the rest of the world is expected to continue for some time to come. Market volatility is expected to persist as the UK continues its negotiations on a future trade agreement with the EU and its potential future trading partners around the world. Throughout this period, we will continually update our assessment of potential consequences for our customers, products and banking model and re-evaluate our mitigating actions accordingly. The scale and nature of the impact on us will depend on the precise terms on which we and our customers will be able to conduct cross-border business following the end of the transition period.

- Clients: the UK's departure from the EU is likely to impact our CMB clients' operating models, including their supply chains, working capital requirements, investment decisions and financial markets infrastructure access. Some EEA incorporated

clients will be required to be migrated from the UK to HSBC France (or another EEA entity) and most customers, who we expect will no longer be able to be serviced out of the UK, have now been migrated.

- People: the potential loss of freedom of movement could impact our EEA staff resident in the UK.

Our priority is to ensure we continue to support our clients and people through this period of uncertainty, and help minimise any disruption. Changes to the UK's current trade relationships could require changes to our banking model to ensure we continue to comply with law and regulation in meeting the needs of our customers and conducting our business. In addition, any negative impact on the economy, demand for borrowing and capital flows as a result of the aforementioned uncertainty, volatility or result of UK negotiations could have a consequential negative impact on HSBC UK.

The outbreak of coronavirus in mainland China and Hong Kong is being actively monitored to assess any potential economic impact on our clients, our staff or our businesses.

Mitigating actions

- We have undertaken a comprehensive impact assessment of the UK leaving the EU, to understand the range of potential implications for our customers, our products and our business. Where necessary, we have identified actions, including evolving our business models, to ensure we can continue to serve our customers.
- We actively monitor our portfolio to identify areas of stress, supported by stress testing analyses. Vulnerable industry sectors or asset classes are subject to additional management review to determine if any adjustments to risk policy or appetite are required.
- We continue to stay very close to our clients, via proactive communications and dedicated channels to respond to customer queries.
- We will be supporting our EEA staff resident in the UK with their settlement applications.
- We will continue to work with regulators, governments and our clients in an effort to manage risks as they arise, particularly across the most impacted industry sectors.
- We have reviewed our business continuity plans following the coronavirus outbreak to ensure the safety and well-being of our staff and customers, and to ensure our ability to maintain our business operations is upheld.

Turning of the credit cycle

Modest UK economic growth was seen in 2019. Uncertainty continues to exist concerning the impact of the UK's withdrawal from the EU, including the potential impacts of re-negotiated trade related arrangements with the EU and its member states. Retail sales growth in the UK continues to be subdued with increased reports of tightening discretionary spending.

Impairment charges increased in 2019, reflecting a return to more typical levels after a sustained period of unusually benign credit conditions.

Mitigating actions

- We closely monitor economic developments in key markets and sectors and undertake scenario analysis. This enables us to take portfolio actions where necessary, including enhanced monitoring, amending our risk appetite and/or reducing limits and exposures. We also continue to monitor certain high risk portfolios such as retail, construction, commercial real estate and service companies within oil and gas.
- We stress test portfolios of particular concern to identify sensitivity to loss under a range of scenarios, with management actions being taken to rebalance exposures and manage risk appetite where necessary.
- Reviews of key portfolios are undertaken regularly to ensure that individual customer or portfolio risks are understood and our ability to manage the level of facilities offered through any downturn are appropriate. In 2019, we have undertaken specific reviews of portfolios in sectors showing vulnerability such as retail and commercial real estate. For our Retail banking portfolios, detailed performance monitoring is reviewed on a monthly basis, which includes early warning indicators and a view of concentration risks.

Regulatory developments

Financial service providers continue to operate to stringent regulatory and supervisory requirements, particularly in the areas of capital and liquidity management, conduct of business, financial crime, internal risk and control frameworks, the use of models and the integrity of financial services delivery and operational resilience.

The legislative, policy and regulatory change agenda in the financial services sector has been extensive over the past couple of years and the scale of proposed and possible change in this arena is expected to continue into 2020. The areas of potential legislative and regulatory change that may impact HSBC UK in due course include:

- Consumer protection enhancements, including in the economic crime arena and the potential for the FCA to impose a duty of care on financial services providers;
- The possible extension of Open Banking into Open Finance as a means of enhancing competition; and
- Implications resulting from the UK's exit from the EU including through the onshoring of EU law, all of which may affect the activities of HSBC UK.

Mitigating actions

- We are engaged with government, regulatory and industry bodies in the UK to seek to ensure that new requirements are properly considered by regulators and the financial sector and can be implemented in an effective manner.
- We hold regular meetings with UK authorities to discuss strategic contingency plans covering a wide range of scenarios relating to the UK's exit from the EU and what may happen at the end of transition period.

Information security risk and cyber crime

HSBC UK and other organisations continue to operate in an increasingly hostile cyber threat environment, which requires ongoing investment in business and technical controls to defend against these threats.

Key threats include unauthorised access to online customers, advanced malware attacks and distributed denial of service attacks.

Mitigating actions

- We continually evaluate threat levels for the most prevalent attack types and their potential outcomes. To further protect HSBC UK and our customers we strengthened our controls to reduce the likelihood and impact of advanced malware, data leakage, infiltration of payment systems and denial of service attacks. We continue to enhance our cybersecurity capabilities, including threat detection, access control as well as back-up and recovery. An important part of our defence strategy is ensuring our people remain aware of cybersecurity issues and know how to report incidents.
- Cyber risk is a priority area for the Board. We report and review cyber risk and control effectiveness quarterly at executive and non-executive Board level. We also report it across our businesses and functions, to help ensure appropriate visibility and governance of the risk and mitigating actions.
- We participate in law enforcement and industry schemes to share information about tactics employed by cyber-crime groups and to collaborate in fighting, detecting and preventing cyber-attacks on financial organisations.

Ibor transition

Ibors, including sterling Libor, are used to set interest rates on hundreds of trillions of US dollars' worth of different types of financial transactions and are used extensively for valuation purposes, risk measurement and performance benchmarking. In HSBC UK, our key Libor exposure is within our Corporate lending portfolio.

Following the announcement by the FCA in July 2017 that it will no longer persuade or require banks to submit rates for Libor after 2021, the UK market, along with the Bank of England Working Group on Sterling Risk-Free Reference Rates ('RFRWG') has been engaged with facilitating an orderly transition of the relevant Libors to their replacement rates, for example the Sterling Over Night Index Average ('Sonia') for sterling and the Secured Overnight Financing Rate ('SOFR') for US dollars.

The process of developing products that reference the replacement rates and transitioning legacy Ibor contracts exposes HSBC UK to material execution, conduct (and other non-financial risks) and financial risks.

Mitigating actions

- HSBC UK is part of the HSBC Group's global programme to facilitate an orderly transition from Libor for our business and our clients. The UK is a lead market for the required transition activity. In HSBC UK, programme activity is sponsored by the UK CRO, who chairs the UK Ibor transition Project Steering Committee ('PSC').
- The HSBC UK programme is focused on developing alternative rate products that reference the RFRWG's selected replacement rates and making them available to customers. It is also focusing on the supporting processes and systems to develop these products. At the same time, the HSBC UK programme is developing the capability to transition outstanding Libor contracts.
- We have identified a number of potential execution, conduct (and other non-financial risks) and financial risks and we are in the process of addressing these.
- We will continue to engage with industry bodies, regulators and our clients to support an orderly transition.

Climate-related risks

Climate change can impact a number of our risk types:

- Transition Risk, arising from the move to a low-carbon economy, such as through policy, regulatory and technological changes.
- Physical Risk, through increasing severity and/or frequency of severe weather events or other climatic events (e.g. sea level rise, flooding).

These have potential to cause both idiosyncratic and systemic risks, resulting, over time, in potential financial impacts for HSBC UK. Impacts could materialise through higher RWAs, greater transactional losses and/or increased capital requirements. HSBC UK is developing a structured approach to Climate Risk management, in conjunction with the HSBC Group.

The awareness of climate risk, regulatory expectations and reputational risk have all heightened through 2019. The exposure we have to the risk and materialisation of the risk have not materially heightened.

Mitigating actions

- We are considering transition risk from three perspectives: understanding our exposure to transition risk; understanding how our clients are managing transition risk; and measuring our client's progress in reducing carbon emissions. For wholesale credit portfolios, we are using questionnaires to assess transition risk across six sectors. For our retail credit portfolio, we review mortgage exposures on a geographical basis in respect of natural hazard risk and mitigants. For operational risk, we are working with our property insurers to understand geographical exposure of the property portfolio and assess effectiveness of controls for design resilience, operations and business continuity.
- HSBC UK, as part of a wider HSBC Group exercise continues to expand its thinking with regard to stress testing of climate risks. It has commenced sector specific scenario analysis and continues current work to source data and develop scenarios.
- We have public and internal policies for certain sectors which pose us sustainability risk. These include policies on energy, agricultural commodities, chemicals, forestry, mining and metals, and UNESCO World Heritage sites and Ramsar-designated wetlands.
- Our enterprise risk management framework continues to be enhanced to develop and embed the measurement, monitoring and management of climate-related risks.
- An internal HSBC UK Climate Risk Management Meeting provides oversight by seeking to develop risk frameworks in order to protect our UK businesses and clients from climate related risks.
- In line with the PRA requirements we have assigned responsibility for Climate Risk to relevant Senior Management Function ('SMF') holders. Additionally, risk stewards will consider physical and transition risks from climate change relevant to their specific risk function.
- The HSBC Group is working with the PRA, FCA and wider industry through their Climate Financial Risk Forum to ensure it remains aware of and drives emerging best practice.

Internally driven

People risk

Our colleagues are critical to our success and it is important that we identify, manage and mitigate any risks that might have an impact on our colleagues feeling empowered and able to thrive in their careers, as well as being able to support our customers and the communities they serve. We aim to foster a culture that proactively promotes the right colleague behaviours and conduct, and that we have the right number of people with the right skills, knowledge and capabilities to be able to do the right thing for customers.

We proactively engage with regulators and policy makers to help ensure that regulatory changes are implemented effectively. Potential capability issues associated with the changes announced by the Government relating to the use of contractors (IR35) continues to be managed closely.

We continue to increase our focus on resource planning and employee retention to ensure we mitigate any risks around capacity and capability, as well as equipping line managers with the skills to both manage change and support their colleagues to ensure we engender a strong positive culture. Ongoing work continues to ensure we are fully prepared for what might happen at the end of the transition period, following the UK's exit from the EU. Impacted colleagues have received the appropriate support to gain settlement status in the UK where appropriate.

Mitigating actions

- We have processes in place to identify where behaviours and conduct give us cause for concern and can mitigate the risk accordingly.
- HSBC University is focused on the development of our colleagues and supporting our leaders to create an environment for success. This is critical to retaining high-calibre individuals with the values, skills and experience for current and future roles.

IT systems infrastructure and resilience

The HSBC Group is committed to investing in the reliability and resilience of its IT systems and critical services, many of which are relied upon by HSBC UK. The HSBC Group does so in order to protect its customers and ensure they do not receive disruption to services, which could result in reputational and regulatory damage.

Mitigating actions

- We are continuing to invest in transforming how software solutions are developed, delivered and maintained, with a particular focus on providing high-quality, stable and secure services. As part of this, we are concentrating on materially improving system resilience and service continuity testing. We have enhanced the security features of our software development life cycle and improved our testing processes and tools.
- We continue to invest in our fraud systems and controls.
- During 2019, we upgraded many of our IT systems, simplifying our service provision and replacing older IT infrastructure and applications.

Execution risk

In order to deliver our strategic objectives and meet mandatory regulatory requirements, it is important for the bank to maintain a strong focus on execution risk. This requires robust management of significant resource-intensive and time-sensitive programmes. Risks arising from the magnitude and complexity of change may include regulatory censure, reputational damage or financial losses. Current major initiatives include managing the operational implications of the UK leaving the EU on HSBC UK; Ibor transition and the continued development of Open Banking.

Mitigating actions

- Our prioritisation and governance processes for significant projects are monitored by the HSBC UK Executive Committee.
- In 2019, we continued to manage execution risk through closely monitoring the punctual delivery of critical initiatives, internal and external dependencies, and key risks, to allow better portfolio management.

Model risk

Models are used in both financial and non-financial contexts. Model risk arises whenever business decision making includes reliance on models. HSBC UK uses models in a range of business applications, in activities such as customer selection, product pricing, financial crime transaction monitoring, creditworthiness evaluation and financial reporting.

In 2019, we elevated model risk to the highest level within our risk management framework, in reflection of its increasing importance. We have undertaken a number of initiatives to strengthen the Model Risk Management sub-function, including:

Mitigating actions

- We are investing increased resources in the HSBC UK Model Risk Management Function.
- We refined the model risk policy to enable a more risk-based approach to Model Risk Management.
- We designed a new target operating model for Model Risk Management, informed by internal and industry best practice. This will drive the evolution of the overall governance framework to ensure best practice.
- We are refreshing the existing model risk controls to enable better understanding of control objectives and to provide the modelling areas with implementation guidance to enhance effectiveness.

Conduct and customer detriment

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

Mitigating actions

- We also integrated our operational risk and conduct frameworks to better assess and mitigate conduct risks.
- We have continued to enhance our management of conduct in areas including our governance of product arrangements, the treatment of potentially vulnerable customers and encouragement of a 'Speak Up' culture and management of related third party risks.

Financial crime and fraud risk

Throughout 2019, HSBC UK continued to implement the final elements of the Global Standards programme to integrate our anti-money laundering and sanctions capabilities into our day-to-day operations. We continue to enhance our financial crime risk management capabilities and the effectiveness of our financial crime controls, with the HSBC Group maintaining its investment in the next generation of tools to fight financial crime through the application of advanced analytics and artificial intelligence.

Financial institutions remain under considerable regulatory scrutiny regarding their ability to prevent and detect financial crime. There is an increased regulatory focus on fraud and anti-bribery and corruption controls, with expectations that banks should do more to protect customers from fraud and identify and manage bribery and corruption risks within their businesses. Financial crime threats continue to evolve, often in tandem with geopolitical developments. The highly speculative, volatile and opaque nature of virtual currencies, including the pace of development in this area, create challenges in effectively managing financial crime risks. The evolving regulatory environment continues to present execution challenge. The HSBC Group continues to see increasing challenges presented by national data privacy requirements in a global organisation, which may affect its ability to effectively manage financial crime risks.

In December 2012, among other agreements, HSBC Holdings plc ('HSBC Holdings') agreed to an undertaking with the UK Financial Services Authority, which was replaced by a Direction issued by the UK Financial Conduct Authority ('FCA') in 2013, and consented to a cease-and-desist order with the US Federal Reserve Board ('FRB'), both of which contained certain forward-looking anti-money laundering ('AML') and sanctions-related obligations. HSBC also agreed to retain an independent compliance monitor (who is, for FCA purposes, a 'Skilled Person' under section 166 of the Financial Services and Markets Act and, for FRB purposes, an 'Independent Consultant') to produce periodic assessments of the Group's AML and sanctions compliance programme (the 'Skilled Person/Independent Consultant'). In December 2012, HSBC Holdings also entered into an agreement with the Office of Foreign Assets Control ('OFAC') regarding historical transactions involving parties subject to OFAC sanctions. Reflective of the HSBC Group's significant progress in strengthening its financial crime risk management capabilities, the HSBC Group's engagement with the current Skilled Person will be terminated and a new Skilled Person with a narrower mandate will be appointed to assess the remaining areas that require further work in order for the HSBC Group, including HSBC UK, to transition fully to business-as-usual financial crime risk management. The Independent Consultant will continue to carry out an annual OFAC compliance review at the FRB's discretion. The role of the Skilled Person/Independent Consultant is discussed on page 51.

Mitigating actions

- We continue to enhance our financial crime risk management capabilities. We are investing in next generation capabilities to fight financial crime through the application of advanced analytics and artificial intelligence.
- We are strengthening and investing in our fraud controls, to introduce next generation anti-fraud capabilities to protect both customers and the bank.
- We continue to embed our improved Anti-Bribery and Corruption policies and controls, focusing on conduct.
- We continue to educate our staff on emerging digital landscapes and associated risks.

- We have developed procedures and controls to manage the risks associated with direct and indirect exposure to virtual currencies, and we continue to monitor external developments:
- We continue to collaborate with government and law enforcement agencies to address data privacy challenges through international standards, guidance, and legislation to enable effective management of financial crime risk.
- We continue to take steps designed to ensure that the reforms we have put in place are both effective and sustainable over the long-term.

Data management

HSBC UK uses a large number of systems and applications to support key business processes and operations. As a result, we often need to reconcile multiple data sources, including customer data sources, to reduce the risk of error. We, along with other organisations, also need to meet external/ regulatory obligations such as the General Data Protection Regulation ('GDPR'), Basel Committee for Banking Supervision ('BCBS') 239, and Basel III.

Mitigating actions

- We are progressively improving data quality across a large number of systems. Our data management, aggregation and oversight continues to strengthen and enhance the effectiveness of internal systems and processes. We are implementing data controls for critical processes in the 'front-office' systems to improve our data capture at the point of entry. The HSBC Group has achieved its objective of meeting a 'largely compliant' rating in support of the BCBS 239 principles and have now embedded them across the key markets and regions. Embedding of these data controls and best practices ensures that our customer experience and regulatory requirements become more consistent, timely and accurate.
- Through HSBC Group's Global Data Management Framework, we are expanding and enhancing our data governance processes to proactively monitor critical customer, product and transaction data and resolving associated data issues in a timely manner. We have also implemented data controls in order to improve the reliability of data used by our customers and staff.
- We are modernising our data and analytics infrastructure through investments in advanced capabilities in cloud visualisation, machine learning and artificial intelligence platforms.
- In order to protect customer data, we have implemented the global Data Privacy Framework that establishes data privacy practices, design principles and guidelines that demonstrate compliance with data privacy laws and regulations where HSBC UK operates, such as GDPR.

To help our employees keep abreast of data management and data privacy laws and regulations we take part in annual data symposiums and data privacy awareness training highlighting its commitment to protect personal data for customers, employees and stakeholders.

Third party risk management

We utilise third parties for the provision of a range of services, in common with other financial service providers. Risks arising from the use of third-party service providers may be less transparent and therefore more challenging to manage or influence. It is critical that we ensure we have appropriate risk management policies, processes and practices. These should include adequate control over the selection, governance and oversight of third parties, particularly for key processes and controls that could affect operational resilience. Any deficiency in our management of risks arising from the use of third parties could affect our ability to meet strategic, regulatory or client expectations and damage our reputation.

Mitigating actions

- We continued to embed our our third party management framework in the first line of defence through a dedicated team. Processes, controls and technology to asses third party service providers against key criteria and associated control monitoring testing and assurance have been deployed.
- A Third Party Risk Steward has been recruited to oversee third party risk management within HSBC UK. Enhanced reporting of third party risk within our governance committees is being progressed.

Areas of special interest

During 2019, a number of areas have been identified and considered as part of our top and emerging risks because of the effect they may have on HSBC UK.

Process of UK withdrawal from the European Union

The UK left the EU on 31 January 2020 and entered into a transition period until 31 December 2020, during which time negotiations will take place on the future relationship between the UK and the EU. At this stage it remains unclear what that relationship will look like, potentially, leaving firms with little time to adapt to changes which may enter into force on 1 January 2021.

Our programme to manage the impact of the UK leaving the EU has now been largely completed. It is based on the assumption of a scenario whereby the UK will no longer have access to the existing passporting or regulatory equivalence framework that supports cross border business.

Legal entity restructuring

Changes in legal entity structure are likely to be minor and limited to our existing branch in Ireland. We previously used our Irish branch, that relied on passporting out of the UK, for the placement of excess EUR deposits. This may no longer be possible post the end of the transition period. To mitigate this, we have on-boarded appropriate counterparties for foreign exchange swaps and repos, which will enable the Balance Sheet Management ('BSM') team in HSBC UK to manage the EUR position in line with how other non-Sterling currencies are managed.

Customer migrations

The UK's departure from the EU is likely to have an impact on our CMB clients' operating models, including their working capital requirements, investment decisions and financial markets infrastructure access. Our priority is to provide continuity of service, and while our intention is to minimise the level of change for our customers, we have engaged with our EEA-incorporated clients to migrate them from the UK to HSBC France, or another EEA entity. We are working in close collaboration with any remaining clients to make the transition as smooth as possible.

Employees

We will support our EEA staff resident in the UK with their settlement applications.

Across the programme, we have made good progress in terms of ensuring we are prepared for whatever may happen at the end of the transition period. However, there remain execution risks, many of them linked to the uncertain outcome of negotiations.

We have carried out detailed reviews of our credit portfolios to determine those sectors and customers most vulnerable to the UK's exit from the EU. For further details, please see 'Impact of UK economic uncertainty on ECL' on page 33.

Ibor transition

The FSB issued a report in 2014 entitled 'Reforming Major Interest Rate Benchmarks'. This report was produced as a result of attempts to manipulate key Ibors and in recognition of a liquidity decline in interbank unsecured markets. Subsequently, regulators and central banks, in various jurisdictions, have convened National Working Groups ('NWG') including the Bank of England RFRWG, to identify replacement rates for Ibors and, where appropriate, to facilitate an orderly transition to these rates. These rates include the Sonia for sterling and the SOFR for US dollars.

The HSBC Group established the Ibor transition programme with the objective of facilitating an orderly transition from Libor and Eonia for the Group and its clients. This global programme oversees the transition effected by each of the Global Businesses and is sponsored by the Group Chief Risk Officer. In the UK, programme activity is sponsored by the UK CRO, who chairs the UK Ibor transition PSC. The programme is currently focussed on developing alternative rate products, that reference the RFRWG's selected replacement rates, and the supporting processes and systems. The resulting execution risks are being closely monitored by the programme.

The programme is concurrently developing the capability to transition, through re-papering, outstanding Libor and Eonia contracts. HSBC UK has around £53.1bn worth of Libor and Eonia contracts, of which approximately £26.9bn is outstanding that matures beyond 2021.

HSBC UK's ability to transition our portfolio of Ibor referenced loans by the end of 2021, is materially dependent on the availability of products that reference the replacement rates (for example, Sonia for Sterling) and on our customers being ready and able to adapt their own processes and systems to accommodate the replacement products. This may give rise to an elevated level of conduct related risks. HSBC UK is engaging with impacted clients to ensure that customers are aware of the risks associated with ongoing transactions in Libor and Eonia linked products as well as the need to transition legacy contracts prior to the end of 2021.

In addition to the conduct and execution risk, the process of adopting new reference rates may expose the group to an increased level of operational and financial risks, such as potential earnings volatility resulting from contract modifications and a large volume of product and associated process changes. Furthermore, the transition to alternative reference rates could have a range of adverse impacts on our business, including legal proceedings or other actions regarding the interpretation and enforceability of provisions in Ibor based contracts and regulatory investigations or reviews in respect of our preparation and readiness for the replacement of Ibors with alternative reference rates.

HSBC UK continues to engage with industry bodies, regulators and our clients to support an orderly transition and the mitigation of the risks resulting from the transition.

Our material banking risks

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

Description of risks – banking operations

Risks	Arising from	Measurement, monitoring and management of risk
Credit risk (see page 24)		
The risk of financial loss if a customer or counterparty fails to meet an obligation under a contract.	Credit risk arises principally from direct lending, trade finance and leasing business, but also from certain other products such as guarantees and derivatives.	Credit risk is: • measured as the amount that could be lost if a customer or counterparty fails to make repayments; • monitored using various internal risk management measures and within limits approved by individuals within a framework of delegated authorities; and • managed through a robust risk control framework that outlines clear and consistent policies, principles and guidance for risk managers.
Capital and liquidity risk (see pages 44 and 52)		
The risk of having insufficient capital, liquidity or funding resources to meet financial obligations and satisfy regulatory requirements, including pension risk.	Capital and liquidity risk arises from changes to the respective resources and risk profiles driven by customer behaviour, management decisions or the external environment.	Capital and liquidity risk is: • measured through appetites set as target and ratios; • monitored and projected through appetites and using stress and scenario testing and; • managed through capital and liquidity resources in conjunction with risk profiles and cashflows.
Market risk (see page 46)		
The risk that movements in market factors, including but not limited to interest rates, credit spreads and foreign exchange rates will reduce our income or the value of our portfolios.	Exposure to market risk is separated into two portfolios: • trading portfolios; and • non-trading portfolios.	Market risk is: • measured using sensitivities, value at risk ('VaR') and stress testing, giving a detailed picture of potential gains and losses for a range of market movements and scenarios, as well as tail risks over specified time horizons; • monitored using VaR sensitivities, stress testing and other measures, including the sensitivity of net interest income and the sensitivity of structural foreign exchange; and • managed using risk limits approved by the risk management meeting ('RMM').
Resilience risk (see page 49)		
Resilience risk is the risk that we are unable to provide critical services to our customers, affiliates, and counterparties as a result of sustained and significant operational disruption.	Resilience risk arises from failures or inadequacies in processes, people, systems or external events. These may be driven by rapid technological innovation, changing behaviours of our consumers, cyber threats and attacks, cross border dependencies, and third party relationships.	Resilience risk is: • measured through a range of metrics with defined maximum acceptable impact tolerances and against our agreed risk appetite; • monitored through oversight of enterprise processes, risks, controls and strategic change programmes; and • managed by continuous monitoring and thematic review.

Description of risks – banking operations

Risks	Arising from	Measurement, monitoring and management of risk
Regulatory compliance risk (see page 50)		
The risk that we fail to observe the letter and spirit of all relevant laws, codes, rules, regulations and standards of good market practice, and incur fines and penalties and suffer damage to our business.	Regulatory compliance risk arises from the risks associated with breaching our duty to our customers and other counterparties, inappropriate market conduct and breaching other regulatory requirements.	Regulatory compliance risk is: • measured by reference to identified metrics, incident assessments, regulatory feedback and the judgement and assessment of our regulatory compliance teams; • monitored against the first line of defence risk and control assessments, the results of the monitoring and control activities of the second line of defence functions, and the results of internal and external audits and regulatory inspections; and • managed by establishing and communicating appropriate policies and procedures, training employees in them, and monitoring activity to assure their observance. Proactive risk control and/or remediation work is undertaken where required.
Financial crime and fraud risk (see page 50)		
The risk that we knowingly or unknowingly help parties to commit or to further potentially illegal activity including both internal and external fraud.	Financial crime and fraud risk arises from day-to-day banking operations.	Financial crime and fraud risk is: • measured by reference to identified metrics, incident assessments, regulatory feedback and the judgement and assessment of our financial crime risk teams; • monitored against our financial crime risk appetite statement and metrics, the results of the monitoring and control activities of the second line of defence functions, and the results of internal and external audits and regulatory inspections; and • managed by establishing and communicating appropriate policies and procedures, training employees in them, and monitoring activity to ensure their observance. Proactive risk control and/or remediation work is undertaken where required.
Model risk (see page 51)		
Model risk is the potential for adverse consequences from business decisions informed by models, which can be exacerbated by errors in methodology, design or the way they are used.	Model risk arises in both financial and non-financial contexts whenever business decision making includes reliance on models.	Model risk is: • measured by reference to model performance tracking and the output of detailed technical reviews, with key metrics including model review statuses and findings; • monitored against model risk appetite statements, insight from the independent review function, feedback from internal and external audits, and regulatory reviews. • managed by creating and communicating appropriate policies, procedures and guidance, training colleagues in their application, and supervising their adoption to ensure operational effectiveness.

Credit risk overview

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

Credit risk management

(Audited)

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

The principal objectives of our credit risk management are:

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

Within HSBC UK, the Credit Risk function is headed by the Chief Risk Officer who reports to the Chief Executive Officer, with a functional reporting line to the Group Chief Risk Officer.

Its responsibilities are:

- to formulate credit policy. Compliance, subject to approved dispensations, is mandatory for all operating companies which must develop local credit policies consistent with group policies that very closely reflect HSBC Group policy;
- to guide operating companies on the group's appetite for credit risk exposure to specified market sectors, activities and banking products and controlling exposures to certain higher-risk sectors;
- to undertake an independent review and objective assessment of risk. Credit risk assesses all credit facilities and exposures over designated limits, prior to the facilities being committed to customers or transactions being undertaken;
- to monitor the performance and management of portfolios across the group;
- to control exposure to sovereign entities, banks and other financial institutions, as well as debt securities which are not held solely for the purpose of trading;
- to set policy on large credit exposures, ensuring that concentrations of exposure by counterparty, sector or geography do not become excessive in relation to the group's capital base, and remain within internal and regulatory limits;
- to maintain and develop the risk rating framework, systems and models through appropriate governance;
- to report on retail portfolio performance, high risk portfolios, risk concentrations, large impaired accounts, impairment allowances and stress testing results and recommendations to HSBC UK's RMM, Risk Committee and Board; and
- to act on behalf of the group as the primary interface, for credit-related issues, with the BoE, the PRA, the FCA, rating agencies, analysts and counterparts in major banks and non-bank financial institutions.

Concentration of credit risk exposure

(Audited)

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

Credit quality of financial instruments

(Audited)

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

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

For debt securities and certain other financial instruments, external ratings have been aligned to the five quality classifications based upon the mapping of related customer risk rating ('CRR') to external credit rating.

Wholesale lending

The CRR 10-grade scale summarises a more granular underlying 23-grade scale of obligor probability of default ('PD'). All corporate customers are rated using the 10- or 23-grade scale, depending on the degree of sophistication of the Basel approach adopted for the exposure.

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

Retail lending

Retail lending credit quality is based on a 12-month point-in-time probability-weighted probability of default ('PD').

Credit quality classification

		Debt securities and other bills	Wholesale lending		Retail lending	
	Footnotes	External credit rating	Internal credit rating	12-month Basel probability of default %	Internal credit rating	12-month probability-weighted PD %
Quality classification	1, 2					
Strong		A- and above	CRR1 to CRR2	0.000–0.169	Band 1 and 2	0.000–0.500
Good		BBB+ to BBB-	CRR3	0.170–0.740	Band 3	0.501–1.500
Satisfactory		BB+ to B and unrated	CRR4 to CRR5	0.741–4.914	Band 4 and 5	1.501–20.000
Sub-standard		B- to C	CRR6 to CRR8	4.915–99.999	Band 6	20.001–99.999
Credit-impaired		Default	CRR9 to CRR10	100.000	Band 7	100.000

1 *Customer risk rating ('CRR').*
2 *12-month point-in-time probability-weighted probability of default ('PD').*

Quality classification definitions

- 'Strong' exposures demonstrate a strong capacity to meet financial commitments, with negligible or low probability of default.
- 'Good' exposures demonstrate a good capacity to meet financial commitments, with low default risk.
- 'Satisfactory' exposures require closer monitoring and demonstrate an average to fair capacity to meet financial commitments, with moderate default risk.
- 'Sub-standard' exposures require varying degrees of special attention and default risk is of greater concern.
- 'Credit-impaired' exposures have been assessed as described on Note 1.2(g) on the financial statements.

Renegotiated loans and forbearance

(Audited)

'Forbearance' describes concessions made on the contractual terms of a loan in response to an obligor's financial difficulties.

A loan is classed as 'renegotiated' when we modify the contractual payment terms on concessionary terms because we have significant concerns about the borrowers' ability to meet contractual payments when due. Non-payment-related concessions (e.g. covenant waivers), while potential indicators of impairment, do not trigger identification as renegotiated loans.

Where customers are in (or approaching) financial difficulty, due consideration is given to provide assistance to customers (either on a temporary or permanent basis) to help them meet the contractual commitments relating to their account. The HSBC UK policy provides guidance on when customers are considered to be in financial difficulty and the various forbearance tools that are available to assist them. It is recognised that customers find themselves in financial difficulties as a result of many different situations and Collections staff speaking with customers will often be best placed to understand the individual circumstances and needs of specific customers. Prior to agreeing a forbearance an appropriate level of assessment on a customer's affordability is completed to ensure any solution agreed with the customer is sustainable.

Refinance risk

Personal lending

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

Wholesale lending

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

Impairment assessment

(Audited)

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

Write-off of loans and advances

(Audited)

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

Personal lending

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

Unsecured personal lending products are normally written off, when there is no realistic prospect of full recovery.

Wholesale lending

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

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

Credit risk in 2019

Dovish global monetary policies remained accommodative through much of 2019, and share indices hit record highs. The Bank of England and the European Central Bank are expected to maintain adequate market liquidity during 2020. Broad corporate credit quality in the UK and Europe has been helped by a record low rate environment despite a lower than expected trend of economic growth. Certain industry segments of the economy are however experiencing market or demand cycle changes that are providing a more challenged market place and this trend is likely to continue going forward. In some areas borrowers have taken on material amounts of new financial leverage leading to more stretched financial profiles. The second order impacts on UK and European corporates of coronavirus are being carefully followed by the bank as this issue develops.

A summary of our current policies and practices regarding credit risk is set out on page 24.

A temporary pause in the issuance of default notices for RBWM accounts took place during 2019, pending changes to policies and processes associated with the issuance of these notices as a result of a review of the Bank's Retail Collections and Recoveries operations. This has resulted in reduced levels of write-off in 2019, and a corresponding increase in Stage 3 balances and ECL. This will be addressed through the recommencement of the default notice process in Q1 2020, which will result in the write-off of balances from Stage 3 and corresponding reductions in ECL.

Re-presentation of gross carrying/nominal amounts staging

The wholesale lending gross carrying/nominal amounts in stages 1 and 2, which were disclosed at 31 December 2018, have been re-presented to reflect the UK economic uncertainty adjustment which was not previously included. In comparison, the allowance for ECL did reflect the UK economic uncertainty adjustment. As a result of the re-presentation, there has been an increase in stage 2 amounts, with a corresponding decrease in stage 1. The 31 December 2018 amounts reflected the probability-weighted view of stage allocation for the consensus scenarios only. The financial instruments and disclosures impacted are as follows:

- Loans and advances to customers: A change of £3,585m comprised of £3,462m for corporate and commercial and £123m non-bank financial institutions.
- Loans and other credit – related commitments: A change of £602m is attributable to £565m for corporate and commercial and £37m for non-bank financial institutions.
- Financial guarantees: A change of £19m comprised of £18m to corporate and commercial and £1m for non-bank financial institutions.
- Commercial real estate lending: A change of £376m.
- Wholesale lending – commercial real estate loans and advances including loan commitments by level of collateral: A change of £493m.
- Wholesale lending – other corporate, commercial and financial (non-bank) loans and advances including loan commitments by level of collateral: A change of £3,743m.

The 'reconciliation of changes in gross carrying/nominal amount and allowances for loans and advances to banks and customers, including loan commitments and financial guarantees' disclosure for 31 December 2018 includes this re-presentation of £4,206m in other movements. There is no impact upon total gross carrying values/nominal amounts, personal lending amounts or allowance for ECL.

Summary of credit risk

The disclosure below presents the gross carrying/nominal amount of financial instruments to which the impairment requirements in IFRS 9 are applied and the associated allowance for ECL.

The allowance for ECL increased from £1,537m at 31 December 2018 to £1,744m at 31 December 2019.

The allowance for ECL at 31 December 2019 comprises £1.679m in respect of assets held at amortised cost and £65m in respect of loan commitments and financial guarantees. There is £1m allowances for ECL in respect of debt instruments measured at fair value through other comprehensive income ('FVOCI').

The following table provides an overview of the group and bank's credit risk exposure. As the majority of the group's financial instruments are held by the bank, the remaining IFRS 7 credit disclosures are provided on a group only basis.

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

(Audited)

	31 Dec 2019		31 Dec 2018	
The group	**Gross carrying/ nominal amount**	**Allowance for ECL[1]**	Gross carrying/ nominal amount	Allowance for ECL[1]
	£m	**£m**	£m	£m
Loans and advances to customers at amortised cost	**184,734**	**(1,678)**	176,266	(1,459)
– personal	**117,669**	**(738)**	110,208	(565)
– corporate and commercial	**64,537**	**(933)**	63,491	(860)
– non-bank financial institutions	**2,528**	**(7)**	2,567	(34)
Loans and advances to banks at amortised cost	**1,390**	**(1)**	1,263	–
Other financial assets measured at amortised costs	**41,871**	**–**	39,142	(3)
– cash and balances at central banks	**37,030**	**–**	33,193	–
– items in the course of collection from other banks	**504**	**–**	603	–
– reverse repurchase agreements – non trading	**3,014**	**–**	3,422	–
– prepayments, accrued income and other assets[2]	**1,323**	**–**	1,924	(3)
Total gross carrying amount on-balance sheet	**227,995**	**(1,679)**	216,671	(1,462)
Loans and other credit related commitments	**63,858**	**(60)**	64,628	(63)
– personal	**37,422**	**(6)**	39,389	(4)
– corporate and commercial	**25,599**	**(54)**	24,884	(59)
– non-bank financial institutions	**837**	**–**	355	–
Financial guarantees	**1,077**	**(5)**	1,284	(12)
– personal	**25**	**–**	16	–
– corporate and commercial	**685**	**(5)**	782	(12)
– non-bank financial institutions	**367**	**–**	486	–
Total nominal amount off-balance sheet[3]	**64,935**	**(65)**	65,912	(75)
At 31 December	**292,930**	**(1,744)**	282,583	(1,537)

	Fair value	**Memorandum allowance for ECL[4]**	Fair value	Memorandum allowance for ECL[4]
	£m	**£m**	£m	£m
Debt instruments measured at fair value through other comprehensive income ('FVOCI')	**19,737**	**(1)**	13,203	–

1 *The total ECL is recognised in the loss allowance for the financial asset unless the total ECL exceeds the gross carrying amount of the financial asset, in which case the ECL is recognised as a provision.*

2 *Includes only those financial instruments which are subject to the impairment requirements of IFRS 9. 'Prepayments, accrued income and other assets' as presented within the consolidated balance sheet on page 72 includes both financial and non-financial assets.*

3 *Represents the maximum amount at risk should the contracts be fully drawn upon and clients default.*

4 *Debt instruments measured at FVOCI continue to be measured at fair value with the allowance for ECL as a memorandum item. Change in ECL is recognised in 'Change in expected credit losses and other credit impairment charges' in the income statement.*

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

(Audited)

The bank	31 Dec 2019		31 Dec 2018	
	Gross carrying/ nominal amount	Allowance for ECL[1]	Gross carrying/ nominal amount	Allowance for ECL[1]
	£m	£m	£m	£m
Loans and advances to customers at amortised cost	175,301	(1,400)	167,130	(1,280)
– personal	110,274	(581)	103,186	(463)
– corporate and commercial	54,691	(813)	53,507	(783)
– non-bank financial institutions	10,336	(6)	10,437	(34)
Loans and advances to banks at amortised cost	4,644	(1)	3,883	–
Other financial assets measured at amortised costs	41,874	–	38,950	–
– cash and balances at central banks	37,020	–	33,187	–
– items in the course of collection from other banks	355	–	457	–
– reverse repurchase agreements – non trading	3,014	–	3,422	–
– prepayments, accrued income and other assets[2]	1,485	–	1,884	–
Total gross carrying amount on-balance sheet	221,819	(1,401)	209,963	(1,280)
Loans and other credit related commitments	49,432	(57)	52,225	(62)
– personal	25,891	(5)	28,009	(3)
– corporate and commercial	23,041	(52)	23,915	(59)
– non-bank financial institutions	500	–	301	–
Financial guarantees	1,066	(5)	1,263	(12)
– personal	15	–	15	–
– corporate and commercial	684	(5)	762	(12)
– non-bank financial institutions	367	–	486	–
Total nominal amount off-balance sheet[3]	50,498	(62)	53,488	(74)
At 31 December	272,317	(1,463)	263,451	(1,354)

	Fair value	Memorandum allowance for ECL[4]	Fair value	Memorandum allowance for ECL[4]
	£m	£m	£m	£m
Debt instruments measured at fair value through other comprehensive income ('FVOCI')	19,737	(1)	13,203	–

1 *The total ECL is recognised in the loss allowance for the financial asset unless the total ECL exceeds the gross carrying amount of the financial asset, in which case the ECL is recognised as a provision.*
2 *Includes only those financial instruments which are subject to the impairment requirements of IFRS 9. 'Prepayments, accrued income and other assets' as presented within the bank's balance sheet on page 75 includes both financial and non-financial assets.*
3 *Represents the maximum amount at risk should the contracts be fully drawn upon and clients default.*
4 *Debt instruments measured at FVOCI continue to be measured at fair value with the allowance for ECL as a memorandum item. Change in ECL is recognised in 'Change in expected credit losses and other credit impairment charges' in the income statement.*

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

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

Summary of credit risk (excluding debt instruments measured at FVOCI) by stage distribution and ECL coverage by industry sector at 31 December 2019

(Audited)

	Gross carrying/nominal amount[1]					Allowance for ECL					ECL coverage %				
	Stage 1	Stage 2	Stage 3	POCI	Total	Stage 1	Stage 2	Stage 3	POCI	Total	Stage 1	Stage 2	Stage 3	POCI	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	%	%	%	%	%
Loans and advances to customers at amortised cost	168,351	13,177	3,179	27	184,734	(214)	(626)	(838)	–	(1,678)	0.1	4.8	26.4	1.2	0.9
– personal	112,398	4,069	1,202	–	117,669	(76)	(385)	(277)	–	(738)	0.1	9.5	23.0	–	0.6
– corporate and commercial	53,843	8,710	1,957	27	64,537	(135)	(238)	(560)	–	(933)	0.3	2.7	28.6	1.2	1.4
– non-bank financial institutions	2,110	398	20	–	2,528	(3)	(3)	(1)	–	(7)	0.1	0.8	5.0	–	0.3
Loans and advances to banks at amortised cost	1,390	–	–	–	1,390	(1)	–	–	–	(1)	0.1	–	–	–	0.1
Other financial assets measured at amortised cost	41,834	28	9	–	41,871	–	–	–	–	–	–	–	–	–	–
Loan and other credit-related commitments	61,059	2,456	341	2	63,858	(27)	(14)	(19)	–	(60)	–	0.6	5.6	0.9	0.1
– personal	36,974	369	79	–	37,422	(6)	–	–	–	(6)	–	–	–	–	–
– corporate and commercial	23,323	2,013	261	2	25,599	(21)	(14)	(19)	–	(54)	0.1	0.7	7.3	0.9	0.2
– financial	762	74	1	–	837	–	–	–	–	–	–	–	–	–	–
Financial guarantee and similar contracts	898	142	37	–	1,077	(2)	(2)	(1)	–	(5)	0.2	1.4	2.7	–	0.5
– personal	25	–	–	–	25	–	–	–	–	–	–	–	–	–	–
– corporate and commercial	534	114	37	–	685	(2)	(2)	(1)	–	(5)	0.4	1.8	2.7	–	0.7
– financial	339	28	–	–	367	–	–	–	–	–	–	–	–	–	–
At 31 Dec 2019	273,532	15,803	3,566	29	292,930	(244)	(642)	(858)	–	(1,744)	0.1	4.1	24.1	1.2	0.6

1 *Represents the maximum amount at risk should the contracts be fully drawn upon and clients default.*

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

Stage 2 days past due analysis at 31 Dec 2019

(Audited)

	Gross carrying amount			Allowance for ECL			ECL coverage %		
	Stage 2	*Of which:*	*Of which:*	Stage 2	*Of which:*	*Of which:*	Stage 2	*Of which:*	*Of which:*
		1 to 29 DPD[1]	*30 and > DPD[1]*		*1 to 29 DPD[1]*	*30 and > DPD[1]*		*1 to 29 DPD[1]*	*30 and > DPD[1]*
	£m	*£m*	*£m*	£m	*£m*	*£m*	%	*%*	*%*
Loans and advances to customers at amortised cost:	13,177	*364*	*212*	(626)	*(43)*	*(48)*	4.8	*11.8*	*22.6*
– personal	4,069	*242*	*149*	(385)	*(35)*	*(41)*	9.5	*14.5*	*27.5*
– corporate and commercial	8,710	*122*	*63*	(238)	*(8)*	*(7)*	2.7	*6.6*	*11.1*
– non-bank financial institutions	398	–	–	(3)	–	–	0.8	–	–
Loans and advances to banks at amortised cost	–	–	–	–	–	–	–	–	–
Other financial assets measured at amortised cost	28	–	–	–	–	–	–	–	–

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

Summary of credit risk (excluding debt instruments measured at FVOCI) by stage distribution and ECL coverage by industry sector at 31December 2018 [2] (continued)

(Audited)

	Gross carrying/nominal amout[1]					Allowance for ECL					ECL coverage %				
	Stage 1	Stage 2	Stage 3	POCI	Total	Stage 1	Stage 2	Stage 3	POCI	Total	Stage 1	Stage 2	Stage 3	POCI	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	%	%	%	%	%
Loans and advances to customers at amortised cost	159,533	14,129	2,604	—	176,266	(247)	(597)	(615)	—	(1,459)	0.2	4.2	23.6	—	0.8
– personal	105,920	3,282	1,006	—	110,208	(71)	(327)	(167)	—	(565)	0.1	10.0	16.6	—	0.5
– corporate and commercial	51,622	10,352	1,517	—	63,491	(170)	(261)	(429)	—	(860)	0.3	2.5	28.3	—	1.4
– non-bank financial institutions	1,991	495	81	—	2,567	(6)	(9)	(19)	—	(34)	0.3	1.8	23.5	—	1.3
Loans and advances to banks at amortised cost	1,262	1	—	—	1,263	—	—	—	—	—	—	—	—	—	—
Other financial assets measured at amortised cost	39,110	23	9	—	39,142	(3)	—	—	—	(3)	—	—	—	—	—
Loan and other credit-related commitments	61,344	2,960	324	—	64,628	(32)	(13)	(18)	—	(63)	0.1	0.4	5.6	—	0.1
– personal	38,994	172	223	—	39,389	(4)	—	—	—	(4)	—	—	—	—	—
– corporate and commercial	22,038	2,745	101	—	24,884	(28)	(13)	(18)	—	(59)	0.1	0.5	17.8	—	0.2
– financial	312	43	—	—	355	—	—	—	—	—	—	—	—	—	—
Financial guarantee and similar contracts	1,098	115	71	—	1,284	(3)	(2)	(7)	—	(12)	0.3	1.7	9.9	—	0.9
– personal	15	1	—	—	16	—	—	—	—	—	—	—	—	—	—
– corporate and commercial	602	111	69	—	782	(3)	(2)	(7)	—	(12)	0.5	1.8	10.1	—	1.5
– financial	481	3	2	—	486	—	—	—	—	—	—	—	—	—	—
At 31 Dec 2018	262,347	17,228	3,008	—	282,583	(285)	(612)	(640)	—	(1,537)	0.1	3.6	21.3	—	0.5

1 Represents the maximum amount at risk should the contracts be fully drawn upon and clients default.
2 During the period, the group has re-presented the wholesale lending stage 1 and stage 2 amount. For further details, see page 26.

Stage 2 days past due analysis at 31 Dec 2018 [2] (continued)

(Audited)

	Gross carrying amount[1]			Allowance for ECL			ECL coverage %		
	Stage 2	*Of which:*	*Of which:*	Stage 2	*Of which:*	*Of which:*	Stage 2	*Of which:*	*Of which:*
		1 to 29 DPD	*30 and > DPD*		*1 to 29 DPD*	*30 and > DPD*		*1 to 29 DPD*	*30 and > DPD*
	£m	*£m*	*£m*	£m	*£m*	*£m*	%	*%*	*%*
Loans and advances to customers at amortised cost:	14,129	*333*	*177*	(597)	*(53)*	*(47)*	4.2	*15.9*	*26.6*
– personal	3,282	*238*	*153*	(327)	*(37)*	*(38)*	10.0	*15.5*	*24.8*
– corporate and commercial	10,352	*95*	*24*	(261)	*(16)*	*(9)*	2.5	*16.8*	*37.5*
– non-bank financial institutions	495	—	—	(9)	—	—	1.8	—	—
Loans and advances to banks at amortised cost	1	—	—	—	—	—	—	—	—
Other financial assets measured at amortised cost	23	—	*1*	—	—	—	—	—	—

1 Days past due ('DPD'). Up to date accounts in Stage 2 are not shown in amounts presented above.
2 During the period, the group has re-presented the wholesale lending stage 1 and stage 2 amount. For further details, see page 26.

Credit exposure

Maximum exposure to credit risk

(Audited)

'Maximum exposure to credit risk' table
The following table presents our maximum exposure before taking account of any collateral held or other credit enhancements (unless such enhancements meet accounting offsetting requirements). The table excludes financial instruments whose carrying amount best represents the net exposure to credit risk; and it excludes equity securities as they are not subject to credit risk. For the financial assets recognised on the balance sheet, the maximum exposure to credit risk equals their carrying amount; for financial guarantees and similar contracts granted, it is the maximum amount that we would have to pay if the guarantees were called upon. For loan commitments and other credit-related commitments, it is generally the full amount of the committed facilities. The offset in the table relates to amounts where there is a legally enforceable right of offset in the event of counterparty default and where, as a result, there is a net exposure for credit risk purposes. However, as there is no intention to settle these balances on a net basis under normal circumstances, they do not qualify for net presentation for accounting purposes. No offset has been applied to off-balance sheet collateral. In the case of derivatives the offset column also includes collateral received in cash and other financial assets.

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

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

Other credit risk mitigants

While not disclosed as an offset in the following 'Maximum exposure to credit risk' table, other arrangements are in place which reduce our maximum exposure to credit risk. These include a charge over collateral on borrowers' specific assets such as residential properties and collateral held in the form of financial instruments that are not held on balance sheet. See Note 22 for further details of collateral in respect of certain loans and advances and derivatives.

Maximum exposure to credit risk

(Audited)

	31 Dec 2019			31 Dec 2018		
The group	**Maximum exposure £m**	**Offset £m**	**Net £m**	Maximum exposure £m	Offset £m	Net £m
Loans and advances to customers held at amortised cost	**183,056**	**(3,804)**	**179,252**	174,807	(3,220)	171,587
– personal	**116,931**	**(26)**	**116,905**	109,643	(88)	109,555
– corporate and commercial	**63,604**	**(3,594)**	**60,010**	62,631	(3,132)	59,499
– non-bank financial institutions	**2,521**	**(184)**	**2,337**	2,533	—	2,533
Loans and advances to banks at amortised cost	**1,389**	**—**	**1,389**	1,263	—	1,263
Other financial assets held at amortised cost	**42,006**	**—**	**42,006**	39,287	—	39,287
– cash and balances at central banks	**37,030**	**—**	**37,030**	33,193	—	33,193
– items in the course of collection from other banks	**504**	**—**	**504**	603	—	603
– reverse repurchase agreements – non-trading	**3,014**	**—**	**3,014**	3,422	—	3,422
– prepayments, accrued income and other assets	**1,458**	**—**	**1,458**	2,069	—	2,069
Derivatives	**121**	**(26)**	**95**	66	(36)	30
Total on-balance sheet exposure to credit risk	**226,572**	**(3,830)**	**222,742**	215,423	(3,256)	212,167
Total off-balance sheet	**70,654**	**—**	**70,654**	73,226	—	73,226
– financial guarantees and similar contracts	**3,413**	**—**	**3,413**	3,483	—	3,483
– loan and other credit-related commitments	**67,241**	**—**	**67,241**	69,743	—	69,743

Concentration of exposures

The diversification of our lending portfolio and our broad range of businesses and products ensured that we did not overly depend on any one business segment to generate growth in 2019.

Loans and advances to customers and banks held at amortised cost

The table on page 39 analyses loans and advances by industry sector to show any concentration of credit risk exposures.

Other financial assets held at amortised cost

Financial investments

Our holdings of government and government agency debt securities, corporate debt securities, asset-backed securities and other securities were spread across a range of issuers in 2019 with 97% (2018: 100%) invested in government or government agency debt securities.

Items in the course of collection from other banks

Settlement risk arises in any situations where a payment in cash, securities or equities is made with the expectation of a corresponding receipt of cash, securities or equities. Daily settlement limits are established for counterparties to cover the aggregate of transactions with each counterparty on any single day.

The group substantially mitigates settlement risk on many transactions, particularly those involving securities, by settling through assured payment systems, or on a delivery-versus-payment basis.

Measurement uncertainty and sensitivity analysis of ECL estimates

The recognition and measurement of ECL involves the use of significant judgement and estimation. We form multiple economic scenarios based on economic forecasts, apply these assumptions to credit risk models to estimate future credit losses, and probability-weight the results to determine an unbiased ECL estimate.

Methodology

We use multiple economic scenarios to reflect assumptions about future economic conditions, starting with three economic scenarios based on consensus forecast distributions, supplemented by alternative or additional economic scenarios and/or management adjustments where, in management's judgement, the consensus forecast distribution does not adequately capture the relevant risks.

The three economic scenarios represent the 'most likely' outcome and two less likely outcomes referred to as the Upside and Downside scenarios. Each outer scenario is consistent with a probability of 10%, while the Central scenario is assigned the remaining 80%, according to the decision of the Group's senior

management. This weighting scheme is deemed appropriate for the unbiased estimation of ECL in most circumstances.

Economic assumptions in the Central consensus economic scenario are set using consensus forecasts which represent the average of forecasts of external economists. Reliance on external forecasts helps ensure that the Central scenario is unbiased and maximises the use of independent information. The Upside and Downside scenarios are selected with reference to externally available forecast distributions and are designed to be cyclical, in that GDP growth, inflation and unemployment usually revert back to the Central scenario after the first three years. We determine the maximum divergence of GDP growth from the Central scenario using the 10th and the 90th percentile of the entire distribution of forecast outcomes. While key economic variables are set with reference to external distributional forecasts, we also align the overall narrative of the scenarios to the macroeconomic risks described in our 'Top and emerging risks' on page 18. This ensures that scenarios remain consistent with the more qualitative assessment of these risks. We project additional variable paths using the external provider's global macro model.

The Upside and Downside scenarios are generated once a year, reviewed at each reporting date to ensure that they are an appropriate reflection of management's view and updated if economic conditions change significantly. The Central scenario is generated every quarter. For quarters without updates to outer scenarios, wholesale and retail credit risk use the updated Central scenario to approximate the impact of the most recent outer scenarios.

Additional scenarios are created as required, to address those forward-looking risks that management consider are not adequately captured by the consensus. At the reporting date, we have deployed additional scenarios to address economic uncertainty.

Description of consensus economic scenarios

The economic assumptions presented in this section have been formed internally by the HSBC Group specifically for the purpose of calculating ECL.

The consensus Central scenario

Our Central scenario is one of moderate growth over the forecast period 2020–2024. Global GDP growth is expected to be 2.8% on average over the period, which is marginally lower than the average growth rate over the period 2014–2018. We note:

- Expected average rates of GDP growth over the 2020–2024 period are lower than average growth rates achieved over the 2014–2018 period. This reflects expectations that the long-term impact of current economic uncertainty will be moderately adverse.
- The unemployment rate is expected to rise over the forecast horizon.
- Inflation is expected to be stable and will remain close to central bank targets in our core markets over the forecast period.
- The Bank of England kept its main policy interest rates in 2019 and is expected to continue to maintain a low interest rate environment over the projection horizon.

The following table describes key macroeconomic variables and the probabilities assigned in the consensus Central scenario applied at 31 December 2019 and 31 December 2018.

Central scenario

	Average 2020–2024	Average 2019–2023
	UK	UK
GDP growth rate (%)	**1.6**	1.7
Inflation (%)	**2.0**	2.1
Unemployment (%)	**4.4**	4.5
Short-term interest rate (%)	**0.6**	1.2
10-year Treasury bond yields (%)	**1.7**	2.6
House price growth (%)	**3.0**	2.9
Equity price growth (%)	**2.8**	3.2
Probability (%)	**55**	50

The consensus Upside scenario

The economic forecast distribution of risks (as captured by consensus probability distributions of GDP growth) has shown a decrease in upside risks over the course of 2019. In the first two years of the Upside scenario, global real GDP growth rises before converging to the Central scenario.

Increased confidence, de-escalation of trade tensions, removal of trade barriers, expansionary fiscal policy, positive resolution of economic uncertainty in the UK, stronger oil prices and a calming of geopolitical tensions are the risk themes that support the Upside scenario.

The following table describes key macroeconomic variables and the probabilities assigned in the consensus Upside scenario applied at 31 December 2019 and 31 December 2018.

Upside scenario

	Average 2020–2024	Average 2019–2023
	UK	UK
GDP growth rate (%)	**2.1**	2.2
Inflation (%)	**2.4**	2.3
Unemployment (%)	**4.0**	4.2
Short-term Interest rate (%)	**0.6**	1.3
10-year Treasury bond yields (%)	**1.7**	2.7
House price growth (%)	**4.4**	4.1
Equity price growth (%)	**4.4**	6.0
Probability (%)	**10**	10

The Downside scenarios

The consensus Downside scenario

The distribution of risks (as captured by consensus probability distributions of GDP growth) has shown a marginal increase in downside risks over the course of 2019 (see discussion on the economic uncertainty below). In the Downside scenario, global real GDP growth declines for two years before recovering towards its long-run trend. House price growth either stalls or contracts and equity markets correct abruptly in our major markets in this scenario. The potential slowdown in global demand would drive commodity prices lower and result in an accompanying fall in inflation. Central banks would be expected to enact loose monetary policy, which in some markets would result in a reduction in the key policy interest rate. The scenario is consistent with our top and emerging risks.

The following table describes key macroeconomic variables and the probabilities assigned in the Consensus Downside scenario applied at 31 December 2019 and 31 December 2018.

Downside scenario

	Average 2020–2024	Average 2019–2023
	UK	UK
GDP growth rate (%)	**1.4**	1.1
Inflation (%)	**1.7**	1.7
Unemployment (%)	**4.8**	4.8
Short Term Interest rate (%)	**0.1**	0.3
10Y Treasury bond Yields (%)	**0.8**	1.6
House price growth (%)	**1.6**	1.0
Equity price growth (%)	**(1.1)**	(0.2)
Probability (%)	**—**	—

Alternative Downside scenarios for the UK

Three alternative Downside scenarios were maintained in 2019 for the UK, reflecting management's view of the distribution of economic risks. These scenarios reflect management's judgement that the consensus distribution does not adequately reflect the risks that stem from the UK's departure from the EU on 31 January 2020. Management evaluated events over the course of 2019 and assigned probabilities to these scenarios that take into consideration all relevant economic and political events. The three scenarios and associated probabilities are described below.

- UK alternative Downside scenario 1: Economic uncertainty could have a large impact on the UK economy resulting in a long-lasting recession with a weak recovery. This scenario reflects the consequences of such a recession with an initial risk-premium shock and weaker long-run productivity growth. This scenario has been used with a 25% weighting.
- UK alternative Downside scenario 2: This scenario reflects the possibility that economic uncertainty could result in a deep cyclical shock triggering a steep depreciation in sterling, a sharp increase in inflation and an associated monetary policy response. This represents a tail risk and has been assigned a 5% weighting.
- UK alternative Downside scenario 3: This scenario reflects the possibility that the adverse impact associated with economic uncertainty currently in the UK could manifest over a far longer period of time with the worst effects occurring later than in the above two scenarios. This scenario is also considered a tail risk and has been assigned a 5% weighting.

The table below describes key macro-economic variables and the probabilities for each of the Alternative Downside scenarios applied at 31 December 2019 and 31 December 2018:

Average 2020–2024

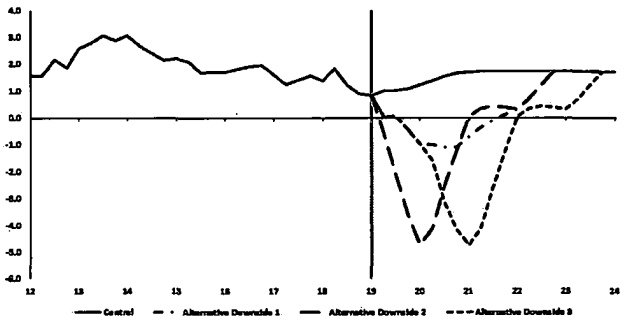
	Alternative Downside scenario 1	**Alternative Downside scenario 2**	**Alternative Downside scenario 3**
GDP growth rate (%)	**0.3**	**(0.3)**	**(0.8)**
Inflation (%)	**2.3**	**2.5**	**2.7**
Unemployment (%)	**6.5**	**8.0**	**7.7**
Short-term interest rate (%)	**0.4**	**2.5**	**2.5**
10-year Treasury bond yields (%)	**1.8**	**4.0**	**4.0**
House price growth (%)	**(1.7)**	**(3.7)**	**(4.8)**
Equity price growth (%)	**(3.3)**	**(4.6)**	**(9.6)**
Probability (%)	**25**	**5**	**5**

Average 2019-2023

	Alternative Downside scenario 1	Alternative Downside scenario 2	Alternative Downside scenario 3
GDP growth rate (%)	0.5	(0.1)	(0.7)
Inflation (%)	2.2	2.4	2.7
Unemployment (%)	6.5	8.0	7.7
Short-term interest rate (%)	0.4	2.5	2.5
10-year Treasury bond yields (%)	1.8	4.0	4.0
House price growth (%)	(1.5)	(3.3)	(4.8)
Equity price growth (%)	(0.9)	(2.3)	(7.5)
Probability (%)	30	5	5

The conditions that resulted in departure from the consensus economic forecasts will be reviewed regularly as economic conditions change in future to determine whether these adjustments continue to be necessary.

The graph below shows the historical and forecasted GDP growth rate for five years for the various economic scenarios.



How economic scenarios are reflected in the wholesale calculation of ECL

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

For impaired loans, LGD estimates take into account independent recovery valuations provided by external consultants where available or internal forecasts corresponding to anticipated economic conditions and individual company conditions. In estimating the ECL on impaired loans that are individually considered not to be significant, we incorporate forward economic guidance proportionate to the probability-weighted outcome and the Central scenario outcome for non-stage 3 populations.

How economic scenarios are reflected in the retail calculation of ECL

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

Impact of UK economic uncertainty on ECL

At 31 December 2019, the impact of using additional scenarios to the consensus distribution to address economic uncertainty was £207m (2018: £258m), consisting of £123m (2018: £126m) in the retail portfolio and £84m (2018: £132m) in the wholesale portfolio. We also considered developments after the balance sheet date and concluded that they did not necessitate any adjustment to the approach or judgements taken on 31 December 2019.

Economic scenarios sensitivity analysis of ECL estimates

Management considered the sensitivity of the ECL outcome against the economic forecasts as part of the ECL governance process by recalculating the ECL under each scenario described above for selected portfolios, applying a 100% weighting to each scenario in turn. The weighting is reflected in both the determination of a significant increase in credit risk and the measurement of the resulting ECL.

The ECL calculated for the Upside and Downside scenarios should not be taken to represent the upper and lower limits of possible

actual ECL outcomes. The impact of defaults that might occur in future under different economic scenarios is captured by recalculating ECL for loans in stages 1 and 2 at the balance sheet date. The population of stage 3 loans (in default) at the balance sheet date is unchanged in these sensitivity calculations. Stage 3 ECL would only be sensitive to changes in forecasts of future economic conditions if the LGD of a particular portfolio was sensitive to these changes.

There is a particularly high degree of estimation uncertainty in numbers representing tail risk scenarios when assigned a 100% weighting, and an indicative range is provided for the UK tail risk sensitivity analysis.

For wholesale credit risk exposures, the sensitivity analysis excludes ECL and financial instruments related to defaulted obligors because the measurement of ECL is relatively more sensitive to credit factors specific to the obligor than future economic scenarios, and it is impracticable to separate the effect of macroeconomic factors in individual assessments.

For retail credit risk exposures, the sensitivity analysis includes ECL for loans and advances to customers related to defaulted obligors. This is because the retail ECL for secured mortgage portfolios including loans in all stages is sensitive to macroeconomic variables.

Wholesale analysis

IFRS 9 ECL sensitivity to future economic conditions[1]

	2019 UK £m	2018 UK £m
ECL of financial instruments subject to significant measurement uncertainty at 31 Dec[2]		
Reported ECL	**430**	491
Consensus scenarios		
Central scenario	**320**	357
Upside scenario	**286**	326
Downside scenario	**378**	411
Alternative scenarios		
UK alternative Downside scenario 1	**580**	534
Tail risk scenarios (UK alternative Downside scenarios 2 and 3)	**1,008-1,115**	891-1,019
Gross carrying/ nominal amount[3]	**137,868**	129,651

1 *Excludes ECL and financial instruments relating to defaulted obligors because the measurement of ECL is relatively more sensitive to credit factors specific to the obligor than future economic scenarios.*
2 *Includes off-balance sheet financial instruments that are subject to significant measurement uncertainty. Also includes low credit risk financial instruments such as Debt instruments at FVOCI which have low ECL coverage ratios under all the above scenarios.*
3 *Includes low credit-risk financial instruments such as Debt instruments at FVOCI, which have low ECL coverage ratios under all the above scenarios.*

The possible impact of Downside scenarios increased over 2019, primarily due to downward revisions in consensus forecasts and their resultant impact on the additional Downside scenarios.

The underlying movement in the reported ECL was driven by changes in the probability weights of the underlying scenarios together with a shift in the portfolio mix of underlying assets. Furthermore, the impact of the additional Downside scenarios, particularly alternative Downside scenario 2 and alternative Downside scenario 3, were relatively more severe than 2018 given marginally weaker than forecast economic performance in 2019.

Retail analysis

IFRS 9 ECL sensitivity to future economic conditions[1]

	2019 UK £m	2018 UK £m
ECL of loans and advances to customers at 31 Dec[2]		
Reported ECL (£m)	**708**	546
Consensus scenarios		
Central scenario	**584**	417
Upside scenario	**519**	370
Downside scenario	**694**	495
Alternative scenarios		
UK alternative Downside scenario 1	**910**	699
Tail risk scenarios (UK alternative Downside scenarios 2 and 3)	**1,138-1,297**	897-1,036
Gross carrying amount (£m)	**113,135**	106,201

1 *ECL sensitivities exclude portfolios utilising less complex modelling approaches.*
2 *ECL sensitivity includes only on balance sheet financial instruments to which IFRS 9 impairment requirements are applied.*

At 31 December 2019, the significant level of retail ECL sensitivity in the retail portfolio was observed due to the interaction between economic forecasts, the quantum of exposures and credit characteristics of the underlying portfolios.

The changes in sensitivity from 31 December 2018 is reflective of changes in lending volumes, credit quality and movements in foreign exchange. The increase in stage 3 ECL is due to a pause in write-offs and changes in credit quality.

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

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

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

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

The 'new financial assets originated or purchased', 'net further lending' and 'assets derecognised (including final repayments)' represent the gross carrying/nominal amount and associated allowance ECL impact from volume movements within the group's lending portfolio.

Reconciliation of changes in gross carrying/nominal amount and allowances for loans and advances to banks and customers including loan commitments and financial guarantees[1, 2, 3]

(Audited)

	Non credit impaired				Credit impaired					
	Stage 1		Stage 2		Stage 3		POCI		Total	
	Gross carrying/ nominal amount	Allowance for ECL	Gross carrying/ nominal amount	Allowance for ECL	Gross carrying/ nominal amount	Allowance for ECL	Gross carrying/ nominal amount	Allowance for ECL	Gross carrying/ nominal amount	Allowance for ECL
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
At 1 Jan 2019	**222,184**	**(283)**	**17,187**	**(611)**	**3,000**	**(640)**	**–**	**–**	**242,371**	**(1,534)**
Transfers of financial instruments:	**(2,733)**	**(227)**	**1,290**	**369**	**1,443**	**(142)**	**–**	**–**	**–**	**–**
– transfers from Stage 1 to Stage 2	**(14,484)**	**53**	**14,484**	**(53)**	**–**	**–**	**–**	**–**	**–**	**–**
– transfers from Stage 2 to Stage 1	**11,873**	**(262)**	**(11,873)**	**262**	**–**	**–**	**–**	**–**	**–**	**–**
– transfers to Stage 3	**(313)**	**2**	**(1,618)**	**188**	**1,931**	**(190)**	**–**	**–**	**–**	**–**
– transfers from Stage 3	**191**	**(20)**	**297**	**(28)**	**(488)**	**48**	**–**	**–**	**–**	**–**
Net remeasurement of ECL arising from transfer of stage	**–**	**193**	**–**	**(138)**	**–**	**(2)**	**–**	**–**	**–**	**53**
New financial assets originated or purchased	**41,977**	**(71)**	**–**	**–**	**–**	**–**	**29**	**–**	**42,006**	**(71)**
Asset derecognised (including final repayments)	**(22,938)**	**21**	**(1,840)**	**78**	**(617)**	**175**	**–**	**–**	**(25,395)**	**274**
Changes to Risk parameters – further lending/ repayment	**(7,621)**	**55**	**(889)**	**38**	**248**	**5**	**–**	**–**	**(8,262)**	**98**
Changes to risk parameters – credit quality	**–**	**66**	**–**	**(377)**	**–**	**(739)**		**–**	**–**	**(1,050)**
Assets written off	**–**	**–**	**–**	**–**	**(472)**	**472**	**–**	**–**	**(472)**	**472**
Credit related modifications that resulted in derecognition	**–**	**–**	**–**	**–**	**(45)**	**11**	**–**	**–**	**(45)**	**11**
Others	**–**	**–**	**–**	**–**	**–**	**3**	**–**	**–**	**–**	**3**
At 31 Dec 2019	**230,869**	**(246)**	**15,748**	**(641)**	**3,557**	**(857)**	**29**	**–**	**250,203**	**(1,744)**
ECL release/(charge) for the period		**264**		**(399)**		**(561)**		**–**		**(696)**
Recoveries										**78**
Others										**5**
Total change in ECL for the period										**(613)**
At 1 Jan 2018	–	–	–	–	–	–	–	–	–	–
Transfer to from HSBC Bank Plc and its subsidiaries	216,026	(288)	9,502	(453)	2,711	(663)	–	–	228,239	(1,404)
Transfers of financial instruments:	(1,336)	(36)	876	90	460	(54)	–	–	–	–
– transfers from Stage 1 to Stage 2	(4,977)	50	4,977	(50)	–	–	–	–	–	–
– transfers from Stage 2 to Stage 1	3,729	(86)	(3,729)	86	–	–	–	–	–	–
– transfers to Stage 3	(143)	6	(462)	65	605	(71)	–	–	–	–
– transfers from Stage 3	55	(6)	90	(11)	(145)	17	–	–	–	–
Net remeasurement of ECL arising from transfer of stage	–	55	–	(54)	–	(1)	–	–	–	–
Net new lending and further lending/payments	12,160	(17)	2,653	53	53	196	–	–	14,866	232
Changes to risk parameters – credit	–	9	–	(250)	–	(352)		–	–	(593)
Assets written off	–	–	–	–	(233)	233	–	–	(233)	233
Others	(4,666)	(6)	4,156	3	9	1	–	–	(501)	(2)
At 31 Dec 2018	222,184	(283)	17,187	(611)	3,000	(640)	–	–	242,371	(1,534)
ECL release/(charge) for the period		47		(251)		(157)		–		(361)
Recoveries										52
Others										4
Total change in ECL for the period										(305)

1 *The Reconciliation excludes loans and advances to other HSBC Group companies. As at 31 December 2019, these amounted to £0.8bn (2018: £0.8bn) and were classified as Stage 1 with no ECL.*

2 *The 31 December 2018 comparative' Reconciliation of changes in gross carrying/nominal amount and allowance for loans and advances to banks and customers' disclosure presents 'New financial assets originated or purchased', 'Assets derecognised (including final repayments)' and 'Changes to risk parameters-further lending/repayments' under' Net new lending and further lending/ repayments'. To provide greater granularity, these amounts have been separately presented in the 31 December 2019 disclosure.*

3 *During the period, the group has re-presented the wholesale lending stage 1 and stage 2 amount. For further details, see page 26.*

Credit quality of financial instruments

(Audited)

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

The five credit quality classifications defined above each encompass a range of granular internal credit rating grades assigned to wholesale and retail lending businesses and the external ratings attributed by external agencies to debt securities, as shown in the table on page 25.

Distribution of financial instruments by credit quality

(Audited)

	Gross carrying/notional amount							
	Strong	Good	Satis-factory	Sub-standard	Credit impaired	Total	Allowance for ECL	Net
	£m	£m	£m	£m	£m	£m	£m	£m
In-scope for IFRS 9								
Loans and advances to customers held at amortised cost	111,802	29,968	35,158	4,600	3,206	184,734	(1,678)	183,056
– personal	104,316	6,339	5,400	412	1,202	117,669	(738)	116,931
– corporate and commercial	6,905	23,002	28,614	4,032	1,984	64,537	(933)	63,604
– non-bank financial institutions	581	627	1,144	156	20	2,528	(7)	2,521
Loans and advances to banks held at amortised cost	1,385	–	5	–	–	1,390	(1)	1,389
Cash and balances at central banks	37,030	–	–	–	–	37,030	–	37,030
Items in the course of collection from other banks	504	–	–	–	–	504	–	504
Reverse repurchase agreements – non-trading	3,014	–	–	–	–	3,014	–	3,014
Other assets	1,063	110	141	–	9	1,323	–	1,323
– endorsements and acceptances	6	52	13	–	–	71	–	71
– accrued income and other	1,057	58	128	–	9	1,252	–	1,252
Debt instruments measured at fair value through other comprehensive income[1]	19,580	–	–	–	–	19,580	(1)	19,579
Out-of-scope for IFRS 9								
Derivatives	84	30	6	1	0	121	–	121
Total gross carrying amount on balance sheet	174,462	30,108	35,310	4,601	3,215	247,696	(1,680)	246,016
Percentage of total credit quality	70.4%	12.2%	14.2%	1.9%	1.3%	100.0%	–	–
Loan and other credit related commitments	36,988	15,950	10,009	568	343	63,858	(60)	63,798
Financial guarantees	381	295	315	49	37	1,077	(5)	1,072
In-scope: Irrecoverable loan commitments and financial guarantees	37,369	16,245	10,324	617	380	64,935	(65)	64,870
Loan and other credit related commitments	429	1,587	1,233	163	32	3,444	–	3,444
Performance and other guarantees	487	903	788	142	31	2,351	(9)	2,342
Out-of-scope: Revocable loan commitments and Non-financial guarantees	916	2,490	2,021	305	63	5,795	(9)	5,786
Total nominal amount off balance sheet	38,285	18,735	12,345	922	443	70,730	(74)	70,656
At 31 Dec 2019	212,747	48,843	47,655	5,523	3,658	318,426	(1,754)	316,672
In-scope for IFRS 9								
Loans and advances to customers held at amortised cost	106,089	26,485	37,827	3,261	2,604	176,266	(1,459)	174,807
– personal	98,679	5,550	4,477	496	1,006	110,208	(565)	109,643
– corporate and commercial	7,009	20,301	31,998	2,666	1,517	63,491	(860)	62,631
– non-bank financial institutions	401	634	1,352	99	81	2,567	(34)	2,533
Loans and advances to banks held at amortised cost	1,254	7	2	–	–	1,263	–	1,263
Cash and balances at central banks	33,193	–	–	–	–	33,193	–	33,193
Items in the course of collection from other banks	603	–	–	–	–	603	–	603
Reverse repurchase agreements – non-trading	3,422	–	–	–	–	3,422	–	3,422
Other assets	1,626	99	189	1	9	1,924	(3)	1,921
– endorsements and acceptances	3	51	31	1	–	86	–	86
– accrued income and other	1,623	48	158	–	9	1,838	(3)	1,835
Debt instruments measured at fair value through other comprehensive income[1]	13,019	–	–	–	–	13,019	–	13,019
Out-of-scope for IFRS 9								
Derivatives	49	15	2	–	–	66	–	66
Assets held for sale	–	–	–	–	–	–	–	–
Total gross carrying amount on balance sheet	159,255	26,606	38,020	3,262	2,613	229,756	(1,462)	228,294
Percentage of total credit quality	69.4%	11.6%	16.5%	1.4%	1.1%	100.0%	–	–
Loan and other credit related commitments	42,745	11,383	9,640	536	324	64,628	(63)	64,565
Financial guarantees	499	239	460	15	71	1,284	(12)	1,272
In-scope: Irrecoverable loan commitments and financial guarantees	43,244	11,622	10,100	551	395	65,912	(75)	65,837
Loan and other credit related commitments	5,178	–	–	–	–	5,178	–	5,178
Performance and other guarantees	232	787	1,111	50	40	2,220	(9)	2,211
Out-of-scope: Revocable loan commitments and Non-financial	5,410	787	1,111	50	40	7,398	(9)	7,389
Total nominal amount off balance sheet	48,654	12,409	11,211	601	435	73,310	(84)	73,226
At 31 Dec 2018	207,909	39,015	49,231	3,863	3,048	303,066	(1,546)	301,520

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

Distribution of financial instruments to which the impairment requirements in IFRS 9 are applied, by credit quality and stage allocation [1]

(Audited)

	Gross carrying/notional amount							
	Strong	Good	Satisfactory	Sub-standard	Credit impaired	Total	Allowance for ECL	Net
	£m	£m	£m	£m	£m	£m	£m	£m
Loans and advances to customers at amortised cost	**111,802**	**29,968**	**35,158**	**4,600**	**3,206**	**184,734**	**(1,678)**	**183,056**
– stage 1	**111,521**	**28,906**	**27,314**	**610**	**–**	**168,351**	**(214)**	**168,137**
– stage 2	**281**	**1,062**	**7,844**	**3,990**	**–**	**13,177**	**(626)**	**12,551**
– stage 3	**–**	**–**	**–**	**–**	**3,179**	**3,179**	**(838)**	**2,341**
– POCI	**–**	**–**	**–**	**–**	**27**	**27**	**–**	**27**
Loans and advances to banks at amortised cost	**1,385**	**–**	**5**	**–**	**–**	**1,390**	**(1)**	**1,389**
– stage 1	**1,385**	**–**	**5**	**–**	**–**	**1,390**	**(1)**	**1,389**
– stage 2	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
– stage 3	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
– POCI	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
Other financial assets measured at amortised cost	**41,611**	**110**	**141**	**–**	**9**	**41,871**	**–**	**41,871**
– stage 1	**41,610**	**109**	**115**	**–**	**–**	**41,834**	**–**	**41,834**
– stage 2	**1**	**1**	**26**	**–**	**–**	**28**	**–**	**28**
– stage 3	**–**	**–**	**–**	**–**	**9**	**9**	**–**	**9**
– POCI	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
Loan and other credit-related commitments	**36,988**	**15,950**	**10,009**	**568**	**343**	**63,858**	**(60)**	**63,798**
– stage 1	**36,859**	**15,785**	**8,304**	**111**	**–**	**61,059**	**(27)**	**61,032**
– stage 2	**129**	**165**	**1,705**	**457**	**–**	**2,456**	**(14)**	**2,442**
– stage 3	**–**	**–**	**–**	**–**	**341**	**341**	**(19)**	**322**
– POCI	**–**	**–**	**–**	**–**	**2**	**2**	**–**	**2**
Financial guarantees	**381**	**295**	**315**	**49**	**37**	**1,077**	**(5)**	**1,072**
– stage 1	**381**	**288**	**206**	**23**	**–**	**898**	**(2)**	**896**
– stage 2	**–**	**7**	**109**	**26**	**–**	**142**	**(2)**	**140**
– stage 3	**–**	**–**	**–**	**–**	**37**	**37**	**(1)**	**36**
– POCI	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
At 31 Dec 2019	**192,167**	**46,323**	**45,628**	**5,217**	**3,595**	**292,930**	**(1,744)**	**291,186**
Debt instruments at FVOCI[2]								
– stage 1	**19,580**	**–**	**–**	**–**	**–**	**19,580**	**(1)**	**19,579**
– stage 2	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
– stage 3	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
– POCI	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
At 31 Dec 2019	**19,580**	**–**	**–**	**–**	**–**	**19,580**	**(1)**	**19,579**
Loans and advances to customers at amortised cost	106,089	26,485	37,827	3,261	2,604	176,266	(1,459)	174,807
– stage 1	105,892	25,393	27,772	476	–	159,533	(247)	159,286
– stage 2	197	1,092	10,055	2,785	–	14,129	(597)	13,532
– stage 3	–	–	–	–	2,604	2,604	(615)	1,989
– POCI	–	–	–	–	–	–	–	–
Loans and advances to banks at amortised cost	1,254	7	2	–	–	1,263	–	1,263
– stage 1	1,253	7	2	–	–	1,262	–	1,262
– stage 2	1	–	–	–	–	1	–	1
– stage 3	–	–	–	–	–	–	–	–
– POCI	–	–	–	–	–	–	–	–
Other financial assets measured at amortised cost	38,846	98	188	1	9	39,142	–	39,142
– stage 1	38,845	97	168	–	–	39,110	–	39,110
– stage 2	1	1	20	1	–	23	–	23
– stage 3	–	–	–	–	9	9	–	9
– POCI	–	–	–	–	–	–	–	–
Loan and other credit-related commitments	42,745	11,383	9,640	536	324	64,628	(63)	64,565
– stage 1	42,651	10,860	7,692	141	–	61,344	(32)	61,312
– stage 2	94	523	1,948	395	–	2,960	(13)	2,947
– stage 3	–	–	–	–	324	324	(18)	306
– POCI	–	–	–	–	–	–	–	–
Financial guarantees	499	239	460	15	71	1,284	(12)	1,272
– stage 1	499	227	370	1	–	1,098	(3)	1,095
– stage 2	–	12	90	14	–	115	(2)	113
– stage 3	–	–	–	–	71	71	(7)	64
– POCI	–	–	–	–	–	–	–	–
At 31 Dec 2018	189,433	38,212	48,117	3,813	3,008	282,583	(1,534)	281,049
Debt instruments at FVOCI[2]								
– stage 1	13,019	–	–	–	–	13,019	–	13,019
– stage 2	–	–	–	–	–	–	–	–
– stage 3	–	–	–	–	–	–	–	–
– POCI	–	–	–	–	–	–	–	–
At 31 Dec 2018	13,019	–	–	–	–	13,019	–	13,019

1 *During the period, the group has re-presented the wholesale lending stage 1 and stage 2 amount. For further details, see page 26.*

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

Credit-impaired loans

(Audited)

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

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

Renegotiated loans and forbearance

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

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

	Stage 1	Stage 2	Stage 3	POCI	Total
	£m	£m	£m	£m	£m
Gross carrying amount					
Personal	–	–	472	–	472
– first lien residential mortgages	–	–	326	–	326
– other personal lending	–	–	146	–	146
Wholesale	292	354	915	27	1,588
– corporate and commercial	292	354	909	27	1,582
– non-bank financial institutions	–	–	6	–	6
At 31 Dec 2019	292	354	1,387	27	2,060
Allowance for ECL					
Personal	–	–	(87)	–	(87)
– first lien residential mortgages	–	–	(31)	–	(31)
– other personal lending	–	–	(56)	–	(56)
Wholesale	(1)	(24)	(277)	–	(302)
– corporate and commercial	(1)	(24)	(277)	–	(302)
– non-bank financial institutions	–	–	–	–	–
At 31 Dec 2019	(1)	(24)	(364)	–	(389)
Gross carrying amount					
Personal	–	–	465	–	465
– first lien residential mortgages	–	–	348	–	348
– other personal lending	–	–	117	–	117
Wholesale	282	234	987	–	1,503
– corporate and commercial	282	234	980	–	1,496
– non-bank financial institutions	–	–	7	–	7
At 31 Dec 2018	282	234	1,452	–	1,968
Allowance for ECL					
Personal	–	–	(59)	–	(59)
– first lien residential mortgages	–	–	(28)	–	(28)
– other personal lending	–	–	(31)	–	(31)
Wholesale	(11)	(17)	(280)	–	(308)
– corporate and commercial	(11)	(17)	(279)	–	(307)
– non-bank financial institutions	–	–	(1)	–	(1)
At 31 Dec 2018	(11)	(17)	(339)	–	(367)

Wholesale lending

This section provides further detail on the products in wholesale loans and advances to customers and banks. Product granularity is also provided by stage.

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

	Gross carrying amount					Allowance for ECL				
	Stage 1	Stage 2	Stage 3	POCI	Total	Stage 1	Stage 2	Stage 3	POCI	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Corporate and commercial	53,843	8,710	1,957	27	64,537	(135)	(238)	(560)	–	(933)
– agriculture, forestry and fishing	3,234	371	89	–	3,694	(7)	(15)	(8)	–	(30)
– mining and quarrying	314	761	2	–	1,077	(1)	(6)	–	–	(7)
– manufacture	6,552	1,261	178	–	7,991	(21)	(36)	(78)	–	(135)
– electricity, gas, steam and air-conditioning supply	451	60	81	–	592	(1)	(2)	(11)	–	(14)
– water supply, sewerage, waste management and remediation	879	21	20	–	920	(2)	(1)	(12)	–	(15)
– construction	2,110	1,514	250	–	3,874	(5)	(21)	(114)	–	(140)
– wholesale and retail trade, repair of motor vehicles and motorcycles	8,156	1,923	272	–	10,351	(14)	(49)	(80)	–	(143)
– transportation and storage	1,469	144	89	–	1,702	(5)	(5)	(39)	–	(49)
– accommodation and food	7,202	432	98	–	7,732	(17)	(17)	(15)	–	(49)
– publishing, audiovisual and broadcasting	1,700	333	33	15	2,081	(9)	(8)	(5)	–	(22)
– real estate	10,703	800	578	–	12,081	(12)	(23)	(109)	–	(144)
– professional, scientific and technical activities	3,238	211	63	–	3,512	(13)	(12)	(34)	–	(59)
– administrative and support services	3,852	569	95	12	4,528	(14)	(23)	(30)	–	(67)
– public administration and defence, compulsory social security	6	7	–	–	13	–	–	–	–	–
– education	784	48	9	–	841	(4)	(3)	(4)	–	(11)
– health and care	1,348	137	75	–	1,560	(5)	(8)	(15)	–	(28)
– arts, entertainment and recreation	908	59	18	–	985	(3)	(5)	(4)	–	(12)
– other services	406	59	7	–	472	(2)	(4)	(2)	–	(8)
– activities of households	–	–	–	–	–	–	–	–	–	–
– assets backed securities	531	–	–	–	531	–	–	–	–	–
Non-bank financial institutions	2,110	398	20	–	2,528	(3)	(3)	(1)	–	(7)
Loans and advances to banks	1,390	–	–	–	1,390	(1)	–	–	–	(1)
At 31 Dec 2019	57,343	9,108	1,977	27	68,455	(139)	(241)	(561)	–	(941)

Total wholesale credit-related commitments and financial guarantees by stage distribution

	Nominal amount					Allowance for ECL				
	Stage 1	Stage 2	Stage 3	POCI	Total	Stage 1	Stage 2	Stage 3	POCI	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Corporate and commercial	23,857	2,127	298	2	26,284	(23)	(16)	(20)	–	(59)
Financial	1,101	102	1	–	1,204	–	–	–	–	–
At 31 Dec 2019	24,958	2,229	299	2	27,488	(23)	(16)	(20)	–	(59)

Total wholesale lending for loans and advances to banks and customers by stage distribution[1]

	Gross carrying amount					Allowance for ECL				
	Stage 1	Stage 2	Stage 3	POCI	Total	Stage 1	Stage 2	Stage 3	POCI	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Corporate and commercial	51,622	10,352	1,517	–	63,491	(170)	(261)	(429)	–	(860)
– agriculture, forestry and fishing	2,370	1,163	75	–	3,608	(8)	(26)	(6)	–	(40)
– mining and quarrying	549	437	70	–	1,056	(3)	(2)	(4)	–	(9)
– manufacture	6,494	1,550	110	–	8,154	(21)	(33)	(36)	–	(90)
– electricity, gas, steam and air-conditioning supply	297	143	23	–	463	(1)	(7)	(7)	–	(15)
– water supply, sewerage, waste management and remediation	961	75	16	–	1,052	(2)	(1)	(11)	–	(14)
– construction	3,382	396	284	–	4,062	(7)	(10)	(113)	–	(130)
– wholesale and retail trade, repair of motor vehicles and motorcycles	7,526	2,180	211	–	9,917	(16)	(48)	(53)	–	(117)
– transportation and storage	1,371	242	18	–	1,631	(5)	(6)	(4)	–	(15)
– accommodation and food	5,439	1,274	87	–	6,800	(25)	(26)	(18)	–	(69)
– publishing, audiovisual and broadcasting	1,592	285	66	–	1,943	(11)	(5)	(39)	–	(55)
– real estate	10,583	823	254	–	11,660	(18)	(26)	(65)	–	(109)
– professional, scientific and technical activities	3,260	421	44	–	3,725	(14)	(21)	(20)	–	(55)
– administrative and support services	3,631	705	111	–	4,447	(17)	(20)	(23)	–	(60)
– public administration and defence, compulsory social security	17	–	–	–	17	–	–	–	–	–
– education	718	152	8	–	878	(6)	(5)	(3)	–	(14)
– health and care	1,140	295	99	–	1,534	(5)	(9)	(18)	–	(32)
– arts, entertainment and recreation	918	132	18	–	1,068	(4)	(6)	(3)	–	(13)
– other services	738	79	23	–	840	(7)	(10)	(6)	–	(23)
– activities of households	1	–	–	–	1	–	–	–	–	–
– assets backed securities	635	–	–	–	635	–	–	–	–	–
Non-bank financial institutions	1,991	495	81	–	2,567	(6)	(9)	(19)	–	(34)
Loans and advances to banks	1,262	1	–	–	1,263	–	–	–	–	–
At 31 Dec 2018	54,875	10,848	1,598	–	67,321	(176)	(270)	(448)	–	(894)

Total wholesale credit-related commitments and financial guarantees by stage distribution[1] (continued)

	Nominal amount					Allowance for ECL				
	Stage 1	Stage 2	Stage 3	POCI	Total	Stage 1	Stage 2	Stage 3	POCI	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Corporate and commercial	22,640	2,856	170	—	25,666	(31)	(15)	(25)	—	(71)
Financial	793	46	2	—	841	—	—	—	—	—
At 31 Dec 2018	23,433	2,902	172	—	26,507	(31)	(15)	(25)	—	(71)

1 *During the period, the group has re-presented the wholesale lending stage 1 and stage 2 amount. For further details, see page 26.*

Commercial real estate

Commercial real estate lending includes the financing of corporate, institutional and high net worth individuals who are investing primarily in income-producing assets and, to a lesser extent, in their construction and development. The business focuses mainly on traditional core asset classes such as retail, offices, light industrial and residential building projects.

Commercial real estate lending[1]

	2019	2018
	£m	£m
Gross loans and advances		
Stage 1	**12,094**	13,196
Stage 2	**1,986**	1,006
Stage 3	**716**	525
POCI	**—**	—
At 31 Dec	**14,796**	14,727
– of which: renegotiated loans	***589***	*560*
Allowance for ECL	**(226)**	(204)

1 *During the period, the Group has re-presented the UK wholesale lending stage 1 and stage 2 amount. For further details, see page 26.*

Refinance risk in commercial real estate

Commercial real estate lending tends to require the repayment of a significant proportion of the principal at maturity. Typically, a customer will arrange repayment through the acquisition of a new loan to settle the existing debt. Refinance risk is the risk that a customer, being unable to repay the debt on maturity, fails to refinance it at commercial rates. We monitor our commercial real estate portfolio closely, assessing indicators for signs of potential issues with refinancing.

Commercial real estate gross loans and advances maturity analysis

	2019	2018
	£m	£m
< 1 year	**7,775**	7,379
1-2 years	**3,661**	3,383
2-5 years	**3,057**	3,673
> 5 years	**303**	292
At 31 Dec	**14,796**	14,727

Collateral and other credit enhancement held

(Audited)

Although collateral can be an important mitigant of credit risk, it is HSBC UK's practice to lend on the basis of the customer's ability to meet their obligations out of their cash flow resources rather than rely on the value of security offered. Depending on the customer's standing and the type of product, facilities may be provided unsecured.

For other lending a charge over collateral is obtained and considered in determining the credit decision and pricing. In the event of a default, the group may utilise the collateral as a source of repayment. Depending on its form, collateral can have a significant financial effect in mitigating exposure to credit risk.

Collateral on loans and advances

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

The collateral measured in the following tables consists of fixed first charges on real estate, and charges over cash and marketable financial instruments. The values in the tables represent the expected market value on an open market basis. No adjustment has been made to the collateral for any expected costs of recovery. Marketable securities are measured at their fair value. Other types of collateral such as unsupported guarantees and floating charges over the assets of a customer's business are not measured in the following tables. While such mitigants have value, often providing rights in insolvency, their assignable value is not sufficiently certain and they are therefore assigned no value for disclosure purposes.The LTV ratios presented are calculated by directly associating loans and advances with the collateral that individually and uniquely supports each facility. When collateral assets are shared by multiple loans and advances, whether specifically or, more generally, by way of an all monies charge, the collateral value is pro-rated across the loans and advances protected by the collateral.

For credit-impaired loans, the collateral values cannot be directly compared with impairment allowances recognised. The LTV figures use open market values with no adjustments. Impairment allowances are calculated on a different basis, by considering other cash flows and adjusting collateral values for costs of realising collateral as explained further on page 84.

Commercial real estate loans and advances

The value of commercial real estate collateral is determined by using a combination of external and internal valuations and physical inspections. For CRR 1–7, local valuation policies determine the frequency of review on the basis of local market conditions because of the complexity of valuing collateral for commercial real estate. For CRR 8–10, almost all collateral would have been revalued within the last three years.

Facilities of a working capital nature are generally not secured by a first fixed charge, and are therefore disclosed as not collateralised.

Wholesale lending: commercial real estate loans and advances including loan commitments by level of collateral (by stage)[1 2]

(Audited)

	2019		2018	
	Gross carrying/ nominal amount £m	ECL coverage %	Gross carrying/ nominal amount £m	ECL coverage %
Stage 1				
Not collateralised	4,143	0.1	5,760	0.2
Fully collateralised	12,742	—	12,388	0.1
LTV ratio:				
– less than 50%	4,469	0.1	5,932	0.1
– 51% to 75%	6,682	—	5,171	0.1
– 76% to 90%	1,247	0.1	823	0.1
– 91% to 100%	344	0.1	462	0.1
Partially collateralised (A):	411	0.1	406	0.1
– *collateral value on A*	*373*		*237*	
Total	17,296	0.1	18,554	0.1
Stage 2				
Not collateralised	1,296	1.2	561	1.5
Fully collateralised	840	1.4	1,043	1.5
LTV ratio:				
– less than 50%	416	2.0	415	2.6
– 51% to 75%	355	0.7	593	0.6
– 76% to 90%	12	6.0	21	2.5
– 91% to 100%	57	0.7	14	8.5
Partially collateralised (B):	224	0.2	47	4.2
– *collateral value on B*	*42*		*16*	
Total	2,360	1.2	1,651	1.6
Stage 3				
Not collateralised	49	92.4	44	90.2
Fully collateralised	305	12.7	206	15.0
LTV ratio:				
– less than 50%	32	6.2	89	24.8
– 51% to 75%	52	4.0	47	6.9
– 76% to 90%	54	4.6	41	3.3
– 91% to 100%	167	19.3	29	14.8
Partially collateralised (C):	383	27.9	218	40.3
– *collateral value on C*	*126*		*108*	
Total	737	25.9	468	33.8
POCI				
Not collateralised	—	—	—	—
Fully collateralised	—	—	—	—
LTV ratio:				
– less than 50%	—	—	—	—
– 51% to 75%	—	—	—	—
– 76% to 90%	—	—	—	—
– 91% to 100%	—	—	—	—
Partially collateralised (D):	—	—	—	—
– *collateral value on D*	—		—	
Total	—	—	—	—
At 31 Dec	20,393	1.1	20,673	1.0

1 *During the period, the group has re-presented the wholesale lending stage 1 and stage 2 amount. For further details, see page 26.*

2 *The 2018 comparative amounts have been re-presented. The impact of these re-presentations is to increase stage 1 not collateralised amounts by £459m, increase fully collateralised amounts by £679m and increase partially collateralised amount by £34m; to increase stage 2 not collateralised amounts by £21m, increase fully collateralised amounts by £295m and increase partially collateralised amount by £6m; and to decrease stage 3 not collateralised amounts by £3m, decrease fully collateralised amounts by £133m and increase partially collateralised amount by £14m.*

Wholesale lending: commercial real estate loans and advances including loan commitments by level of collateral [1]

(Audited)

	2019		2018	
	Gross carrying/ nominal £m	ECL coverage %	Gross carrying/ nominal £m	ECL coverage %
Rated CRR/ PD1 to 7				
Not collateralised	5,437	0.3	6,319	0.3
Fully collateralised	13,524	0.1	13,376	0.2
Partially collateralised (A):	630	0.1	435	0.5
– *collateral value on A*	*411*		*248*	
Total	19,591	0.2	20,130	0.2
Rated CRR/ PD 8				
Not collateralised	2	8.5	2	11.9
Fully collateralised	58	7.6	55	7.2
LTV ratio:				
– less than 50%	21	13.2	25	5.3
– 51% to 75%	18	4.7	12	8.1
– 76% to 90%	11	4.7	5	8.6
– 91% to 100%	8	3.0	13	9.6
Partially collateralised (B):	5	3.0	18	2.3
– *collateral value on B*	*4*		*5*	
Total	65	7.2	75	6.2
Rated CRR/ PD9 to 10				
Not collateralised	49	92.4	44	90.2
Fully collateralised	305	12.7	206	14.9
LTV ratio:				
– less than 50%	32	6.2	89	24.6
– 51% to 75%	52	4.0	47	6.4
– 76% to 90%	54	4.6	41	3.9
– 91% to 100%	167	19.3	29	15.1
Partially collateralised (C):	383	27.9	218	40.2
– *collateral value on C*	*126*		*108*	
Total	737	25.9	468	33.8
At 31 Dec	20,393	1.1	20,673	1.0

1 *The 2018 comparative amounts have been re-presented. The impact of these re-presentations is to increase rated CRR/PD1 to 7 not collateralised amounts by £480m, increase fully collateralised amounts by £1,259m and increase partially collateralised amount by £28m; to decrease rated CRR/PD8 fully collateralised amounts by £285m and increase partially collateralised amount by £12m; and to decrease rated CRR/PD 9 to 10 not collateralised amounts by £3m, decrease fully collateralised amounts by £133m and increase partially collateralised amount by £14m.*

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

(Audited)

Other corporate, commercial and financial (non-bank) loans are analysed separately in the following table. For financing activities in corporate and commercial lending that are not predominantly commercial real estate-oriented, collateral value is not strongly correlated to principal repayment performance.

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

Accordingly, the following table reports values only for customers with CRR 8–10, recognising that these loans and advances generally have valuations that are comparatively recent.

Wholesale lending: other corporate, commercial and financial (non-bank) loans and advances including loan commitments by level of collateral (by stage)[1 2]

(Audited)

	2019		2018	
	Gross carrying/ nominal amount	**ECL coverage**	Gross carrying/ nominal amount	ECL coverage
	£m	**%**	£m	%
Stage 1				
Not collateralised	**40,356**	**0.3**	41,055	0.3
Fully collateralised	**18,775**	**0.1**	14,045	0.2
LTV ratio:				
– less than 50%	**8,000**	**0.1**	5,465	0.2
– 51% to 75%	**6,918**	**0.1**	5,200	0.3
– 76% to 90%	**2,312**	**0.2**	2,138	0.2
– 91% to 100%	**1,545**	**0.1**	1,242	0.1
Partially collateralised (A):	**5,809**	**0.1**	4,598	0.2
– *collateral value on A*	***2,679***		*2,250*	
Total	**64,940**	**0.2**	59,698	0.3
Stage 2				
Not collateralised	**7,164**	**2.4**	8,435	2.2
Fully collateralised	**1,751**	**2.2**	3,087	1.7
LTV ratio:				
– less than 50%	**659**	**2.4**	1,331	2.0
– 51% to 75%	**717**	**2.0**	1,261	1.5
– 76% to 90%	**198**	**2.3**	357	1.3
– 91% to 100%	**179**	**2.0**	138	2.1
Partially collateralised (B):	**1,117**	**1.4**	1,397	1.2
– *collateral value on B*	***279***		*265*	
Total	**10,032**	**2.3**	12,919	2.0
Stage 3				
Not collateralised	**994**	**29.4**	811	30.8
Fully collateralised	**295**	**15.4**	282	8.3
LTV ratio:				
– less than 50%	**58**	**22.3**	89	9.1
– 51% to 75%	**148**	**8.5**	116	2.4
– 76% to 90%	**52**	**29.7**	69	15.4
– 91% to 100%	**37**	**12.2**	8	24.3
Partially collateralised (C):	**234**	**22.3**	145	25.1
– *collateral value on C*	***115***		*82*	
Total	**1,523**	**25.6**	1,238	25.0
POCI				
Not collateralised	**–**	**–**	–	–
Fully collateralised	**–**	**–**	–	–
LTV ratio:				
– less than 50%	**–**	**–**	–	–
– 51% to 75%	**–**	**–**	–	–
– 76% to 90%	**–**	**–**	–	–
– 91% to 100%	**–**	**–**	–	–
Partially Collateralised (D):	**29**	**1.2**	–	–
– *collateral value on D*	***2***		–	
Total	**29**	**1.2**	–	–
At 31 Dec	**76,524**	**1.0**	73,855	1.0

1 *During the period, the group has re-presented the wholesale lending stage 1 and stage 2 amount. For further details, see page 26.*

2 *The 2018 comparative amounts have been re-presented. The impact of these re-presentations is to decrease stage 1 not collateralised amounts by £9,384m, increase fully collateralised amounts by £6,036m and increase partially collateralised amount by £1,171m; to increase stage 2 not collateralised amounts by £2,358m, decrease fully collateralised amounts by £2,612m and increase partially collateralised amount by £809m; and to increase stage 3 not collateralised amounts by £84m, increase fully collateralised amounts by £3m and increase partially collateralised amount by £39m.*

Wholesale lending: other corporate, commercial and financial (non-bank) loans and advances including loan commitments by level of collateral rated CRR/PD 8 to 10 only[1]

(Audited)

	2019		2018	
	Gross carrying/ nominal amount	**ECL coverage**	Gross carrying/ nominal amount	ECL coverage
	£m	**%**		
Rated CRR/ PD 8				
Not collateralised	**208**	**12.9**	238	5.5
Fully collateralised	**77**	**4.9**	44	6.9
LTV ratio:				
– less than 50%	**29**	**5.9**	21	5.9
– 51% to 75%	**25**	**6.1**	20	7.2
– 76% to 90%	**21**	**2.4**	2	12.9
– 91% to 100%	**2**	**2.2**	1	8.4
Partially collateralised (A):	**40**	**4.9**	14	8.9
– *collateral value on A*	***25***		*12*	
Total	***325***	***10.1***	296	5.8
Rated CRR/ PD9 to 10				
Not collateralised	**994**	**29.4**	811	30.8
Fully collateralised	**295**	**15.4**	282	8.3
LTV ratio:				
– less than 50%	**58**	**22.3**	89	9.0
– 51% to 75%	**148**	**8.5**	116	2.4
– 76% to 90%	**52**	**29.8**	69	15.2
– 91% to 100%	**37**	**12.3**	8	24.9
Partially collateralised (B):	**263**	**20.0**	145	25.1
– *collateral value on B*	***117***		*82*	
Total	***1,552***	***25.1***	1,238	25.0
At 31 Dec	**1,877**	**22.5**	1,534	21.3

1 *The 2018 comparative amounts have been re-presented. The impact of these re-presentations is to increase rated CRR/PD8 not collateralised amounts by £34m, increase fully collateralised amounts by £6m and increase partially collateralised amount by £2m; and to increase rated CRR/PD 9 to 10 not collateralised amounts by £84m, increase fully collateralised amounts by £3m and increase partially collateralised amount by £39m.*

Other credit risk exposures

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

- some securities issued by governments, banks and other financial institutions benefit from additional credit enhancement provided by government guarantees that cover the assets;
- debt securities issued by banks and financial institutions include asset-backed securities and similar instruments which are supported by underlying pools of financial assets;
- the group's maximum exposure to credit risk includes financial guarantees and similar arrangements that we issue or enter into, and loan commitments that we are irrevocably committed to. Depending on the terms of the arrangement, we may have recourse to additional credit mitigation in the event that a guarantee is called upon or a loan commitment is drawn and subsequently defaults.

Personal lending

We provide a broad range of secured and unsecured personal lending products to meet customer needs. Personal lending includes advances to customers for asset purchases such as residential property where the loans are secured by the assets being acquired. We also offer unsecured lending products such as overdrafts, credit cards and personal loans. The following table shows the levels of personal lending products in the various portfolios.

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

	Gross carrying amount				Allowance for ECL			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
	£m	£m	£m	£m	£m	£m	£m	£m
By portfolio								
First lien residential mortgages	**99,197**	**1,387**	**880**	**101,464**	**(12)**	**(14)**	**(92)**	**(118)**
– of which: interest only (including offset)	***19,480***	***980***	***143***	***20,603***	***(4)***	***(9)***	***(17)***	***(30)***
Other personal lending	**13,201**	**2,682**	**322**	**16,205**	**(64)**	**(371)**	**(185)**	**(620)**
– other	**7,383**	**1,287**	**163**	**8,833**	**(36)**	**(159)**	**(99)**	**(294)**
– credit cards	**5,818**	**1,395**	**159**	**7,372**	**(28)**	**(212)**	**(86)**	**(326)**
At 31 Dec 2019	**112,398**	**4,069**	**1,202**	**117,669**	**(76)**	**(385)**	**(277)**	**(738)**

Total personal credit-related commitments and financial guarantees by stage distribution

	Nominal amount				Allowance for ECL			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
	£m	£m	£m	£m	£m	£m	£m	£m
At 31 Dec 2019	**36,999**	**369**	**79**	**37,447**	**(6)**	**–**	**–**	**(6)**

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

	Gross carrying amount				Allowance for ECL			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
	£m	£m	£m	£m	£m	£m	£m	£m
By portfolio								
First lien residential mortgages	92,973	930	800	94,703	(7)	(13)	(87)	(107)
– of which: interest only (including offset)	*20,895*	*788*	*100*	*21,783*	*(2)*	*(7)*	*(11)*	*(20)*
Other personal lending	12,947	2,352	206	15,505	(64)	(314)	(80)	(458)
– other	7,138	961	127	8,226	(36)	(133)	(49)	(218)
– credit cards	5,809	1,391	79	7,279	(28)	(181)	(31)	(240)
At 31 Dec 2018	105,920	3,282	1,006	110,208	(71)	(327)	(167)	(565)

Total personal credit-related commitments and financial guarantees by stage distribution

	Nominal amount				Allowance for ECL			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
	£m	£m	£m	£m	£m	£m	£m	£m
At 31 Dec 2018	39,009	173	223	39,405	(4)	–	–	(4)

Mortgage lending

We offer a wide range of mortgage products designed to meet customer needs, including capital repayment, interest-only and offset mortgages. Internal credit policies prescribe the range of acceptable residential property LTV thresholds with the maximum upper limit for new loans set between 50% and 95%, depending on the product type and loan amount.

The quality of our mortgage book remained high, with negligible defaults and impairment allowances. The average LTV ratio on new lending was 67%, compared with an estimated 51% for the overall mortgage portfolio.

Exposure to UK interest-only mortgage loans

The following information is presented for the bank's HSBC branded UK interest-only mortgage loans with balances of £11.0bn; this excludes offset mortgages in first direct, private banking mortgages, endowment mortgages and other products.

At the end of 2019, the average LTV ratio in the portfolio was 42%, and 99% of mortgages had an LTV ratio of 75% or less.

Of the interest-only mortgages that expired in 2017, 86% were repaid within 12 months of expiry with a total of 95% being repaid within 24 months of expiry. For interest-only mortgages expiring during 2018, 91% were fully repaid within 12 months of expiry.

The profile of maturing UK interest-only loans is as follows:

UK interest-only mortgage loans

	£m
Matured interest-only mortgage loans[1]	**120**
Interest-only mortgage loans by maturity	**10,903**
– 2020	**231**
– 2021	**329**
– 2022	**325**
– 2023	**421**
– 2024–2028	**2,345**
– post 2028	**7,252**
At 31 Dec 2019	**11,023**

1 *Includes interest-only mortgages which have reached their contractual maturity date, but were unsettled at the end of 2019.*

Other personal lending

Other personal lending consists of credit cards, personal loans and overdrafts.

Collateral and other credit enhancements held

(Audited)

The following table provides a quantification of the value of fixed charges we hold over specific assets where we have a history of enforcing, and are able to enforce, collateral in satisfying a debt in the event of the borrower failing to meet its contractual obligations, and where the collateral is cash or can be realised by sale in an established market. The collateral valuation excludes any adjustments for obtaining and selling the collateral and, in particular, loans shown as not collateralised or partially collateralised may also benefit from other forms of credit mitigants.

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

(Audited)

	2019		2018	
	Gross carrying/ nominal amount	**ECL coverage**	Gross carrying/ nominal amount	ECL coverage
	£m	**%**	£m	%
Stage 1				
Fully collateralised	**105,857**	**–**	99,849	–
LTV ratio:				
– less than 50%	**52,213**	**–**	51,341	–
– 51% to 60%	**16,292**	**–**	16,127	–
– 61% to 70%	**14,796**	**–**	13,463	–
– 71% to 80%	**13,131**	**–**	11,608	–
– 81% to 90%	**8,289**	**–**	6,819	–
– 91% to 100%	**1,136**	**–**	491	–
Partially collateralised (A):	**243**	**–**	275	–
LTV ratio:				
– 101% to 110%	**67**	**0.1**	85	–
– 111% to 120%	**36**	**–**	35	–
– greater than 120%	**140**	**–**	155	–
– *collateral value on A*	***174***		*209*	
Total	**106,100**	**–**	100,124	–
Stage 2				
Fully collateralised	**1,426**	**0.9**	928	1.3
LTV ratio:				
– less than 50%	**852**	**0.7**	703	0.9
– 51% to 60%	**169**	**1.4**	84	3.0
– 61% to 70%	**197**	**1.2**	82	2.2
– 71% to 80%	**175**	**1.0**	31	3.3
– 81% to 90%	**27**	**2.9**	21	3.1
– 91% to 100%	**6**	**1.1**	7	2.4
Partially collateralised (B):	**17**	**1.7**	1	7.6
LTV ratio:				
– 101% to 110%	**15**	**1.3**	–	–
– 111% to 120%	**1**	**3.6**	1	3.4
– greater than 120%	**1**	**4.6**	–	–
– *collateral value on B*	***15***		*1*	–
Total	**1,443**	**0.9**	929	1.4
Stage 3				
Fully collateralised	**876**	**9.9**	783	10.7
LTV ratio:				
– less than 50%	**527**	**7.8**	486	7.8
– 51% to 60%	**119**	**10.0**	118	11.3
– 61% to 70%	**102**	**10.6**	91	18.6
– 71% to 80%	**74**	**19.1**	54	14.9
– 81% to 90%	**36**	**12.1**	26	19.2
– 91% to 100%	**18**	**25.3**	8	35.2
Partially collateralised (C):	**19**	**27.2**	18	15.8
LTV ratio:				
– 101% to 110%	**8**	**19.6**	7	16.0
– 111% to 120%	**5**	**21.7**	4	25.8
– greater than 120%	**6**	**42.9**	7	10.0
– *collateral value on C*	***18***		*14*	
Total	**895**	**10.3**	801	10.9
At 31 Dec	**108,438**	**0.1**	101,854	0.1

Liquidity and funding risk management

Overview

Liquidity risk is the risk that we do not have sufficient financial resources to meet our obligations as they fall due. Liquidity risk arises from mismatches in the timing of cash flows.

Funding risk arises when funding cannot be raised except at excessive cost.

Key developments in 2019

We have amended the Board Risk Appetite Statement to remove the depositor concentration and term contractual maturity limits. Both these risks will be monitored and controlled at the Asset and Liability Committee ('ALCO') level.

We have transferred second-line of defence activities to a newly created team in the Risk function. This team provides independent review and challenge of first-line business activities and approves the liquidity and funding risk management framework ('LFRF').

ILAAP and risk appetite

We maintain a comprehensive LFRF, which aims to enable us to withstand very severe liquidity stresses. The LFRF comprises policies, metrics and controls designed to ensure that management have oversight of our liquidity and funding risks in order to manage them appropriately.

We manage liquidity and funding risk to meet internal minimum requirements and any applicable regulatory requirements at all times. These requirements are assessed through the internal liquidity adequacy assessment process ('ILAAP') which is used to

ensure that we have robust strategies, policies, processes and systems for the identification, measurement, management and monitoring of liquidity risk over an appropriate set of time horizons, including intraday, so as to ensure we maintain adequate levels of liquidity buffers. It informs the validation of risk tolerance and the setting of risk appetite. It also assesses our capability to effectively manage liquidity and funding. These metrics are set and managed locally but are subject to robust global review and challenge to ensure consistency of approach and application of the LFRF across the Group.

Performance and measurement

Funding and liquidity plans form part of the annual operating plan that is approved by the Board with the Board level appetite measures being the liquidity coverage ratio ('LCR') and net stable funding ratio ('NSFR'). An appropriate funding and liquidity profile is managed through a wider set of measures:

- minimum LCR requirement;
- minimum NSFR requirement;
- depositor concentration limit;
- 3-month and 12-month cumulative rolling term contractual maturity limits covering deposits from banks, deposits from non-bank financial institutions and securities issued;
- minimum LCR requirement by currency;
- intra-day liquidity;
- application of liquidity funds transfer pricing; and
- forward-looking funding assessments.

Risks to liquidity and funding

Risks to liquidity and funding are assessed through forecasting, stress testing and scenario analysis combined with ongoing assessments of risks in the business and external environment.

Stress testing, recovery and contingency planning

We use stress testing to evaluate the robustness of plans and risk portfolios, inform the ILAAP and support recovery planning as well as meeting the requirements for stress testing set by regulators. It is an important methodology used to evaluate how much funding and liquidity we require in setting risk appetite.

We maintain contingency plans which can be enacted in the event of internal or external triggers which threaten the liquidity or funding position. We also have established recovery plans addressing the actions that management would consider taking in a stress scenario if the position deteriorates and threatens to breach risk appetite and regulatory minimum levels. The recovery plans set out a range of appropriate actions which could feasibly be executed in a stressed environment to recover the liquidity and funding position.

Liquidity and funding risk in 2019

Liquidity metrics

At 31 December 2019, we were above regulatory minimum levels.

We maintain sufficient unencumbered liquid assets to comply with regulatory requirements. The liquidity value of these liquid assets is shown in the table below along with the LCR level on a European Commission ('EC') basis.

We maintain sufficient stable funding relative to the required stable funding assessed using the NSFR.

Our liquidity and funding position in as at the end of 2019 is analysed in the following sections.

HSBC UK liquidity group[1]

	At	
	31 Dec 2019	31 Dec 2018
LCR (%)	**165**	143
HQLA[2] (£m)	**56,822**	46,357
Net Outflows (£m)	**34,355**	32,442
NSFR (%)	**150**	144

1 *HSBC UK Liquidity Group comprises: HSBC UK Bank plc (including Dublin branch), Marks and Spencer Financial Services plc, HSBC Trust Company (UK) Limited and HSBC Private Bank (UK) Limited. It is managed as a single operating entity, in line with the application of UK liquidity regulation as agreed with the PRA.*

2 *In 2019, the group disclosed HQLA on a weighted basis, 2018 comparatives have been presented on the same basis.*

Liquid assets

As at 31 December 2019 we had a total of £56,822m of highly liquid unencumbered LCR eligible liquid assets (31 December 2018: £46,357m) held in a range of asset classes and currencies. Of these, 99% were eligible as level 1 (31 December 2018: 98%).

The below tables reflects the composition of the liquidity pool by asset type and currency at 31 December 2019:

	Liquidity pool	Cash	Level 1	Level 2
	£m	£m	£m	£m
Cash and balance at central bank	**36,385**	**36,385**	**–**	**–**
Central and local government bonds	**17,545**	**–**	**17,415**	**130**
Regional government PSE	**428**	**–**	**254**	**174**
International organisation and MDBs	**749**	**–**	**749**	**–**
Covered bonds	**429**	**–**	**239**	**190**
Other	**1,286**	**–**	**1,286**	**–**
Total at 31 Dec 2019[1]	**56,822**	**36,385**	**19,943**	**494**
Total at 31 Dec 2018[1]	*46,357*	*32,421*	*12,897*	*1,039*

1 *In 2019 the group disclosed HQLA on a weighted basis, 2018 comparatives have been presented on the same basis.*

	£	$	€	Other	Total
	£m	£m	£m	£m	£m
Liquidity pool at 31 Dec 2019	**45,886**	**6,365**	**4,424**	**147**	**56,822**
Liquidity pool at 31 Dec 2018	38,571	4,820	1,981	985	46,357

Sources of funding

Our primary sources of funding are customer current accounts and customer savings deposits payable on demand or at short notice. The following 'Funding sources and uses' table provides a consolidated view of how our balance sheet is funded, and should be read in light of the LFRF, which requires we manage liquidity and funding risk on a stand-alone basis.

The table analyses our consolidated balance sheet according to the assets that primarily arise from operating activities and the sources of funding primarily supporting these activities. In 2019, the level of customer accounts exceeded the level of loans and advances to customers. The positive funding gap was predominantly deployed in liquid assets, cash and balances with central banks and financial investments, as required by the LFRF.

Funding Sources

	2019 £m	2018 £m
Sources		
Customer accounts	**216,214**	204,837
Deposits by banks	**529**	1,027
Repurchase agreements – non-trading	**98**	639
Debt securities in issue	**3,142**	—
Accruals, deferred income and other liabilities	**27**	35
– Cash collateral, margin and settlement accounts	**27**	35
Subordinated liabilities	**9,533**	4,937
Total equity	**22,251**	22,333
Other balance sheet liabilities	**5,308**	5,131
At 31 Dec	**257,102**	238,939

Funding Uses

	2019 £m	2018 £m
Uses		
Loans and advances to customers	**183,056**	174,807
Loans and advances to banks	**1,389**	1,263
Reverse repurchase agreements – non-trading	**3,014**	3,422
Prepayments, accrued income and other assets[1]	**123**	338
– Cash collateral, margin and settlement accounts	**123**	338
Financial investments	**19,737**	13,203
Cash and balances with Central banks	**37,030**	33,193
Other balance sheet assets	**12,753**	12,713
At 31 Dec	**257,102**	238,939

1 *Includes only those financial instruments that are subject to the impairment requirements of IFRS 9. 'Prepayments, accrued income and other assets' as presented within the consolidated balance sheet on page 72 includes both financial and non-financial assets.*

Pension risk

Governance and structure

A global pension risk framework and accompanying global policies on the management of risks related to defined benefit and defined contribution plans are in place. Pension risk is managed by a network of local and regional pension risk forums. During 2H19, the European Pension Oversight Forum, which previously covered UK and Europe, was split into two and a new Pension Oversight Forum ('POF') established to cover just the HSBC Bank (UK) Pension Scheme, named the UK POF. The HSBC UK Chief Risk Officer remains as Chair of the UK POF, and the Forum is responsible for the governance and oversight of all pension plans sponsored by HSBC UK.

The HSBC UK section of the HSBC Bank (UK) Pension Scheme is an occupational pension scheme as defined by the Pension Schemes Act 1993. It is set up under trust and the assets are held separately to those of HSBC UK. It is regulated by the Pensions Regulator.

Key risk management processes

In the UK, all future pension benefits are provided on a defined contribution basis. A defined benefit pension plan remains in respect of past service. The defined benefit pension plan is sectionalised to ensure no entities outside the ring-fence participate in the same section as HSBC UK.

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

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

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

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

To fund the benefits associated with HSBC UK's section of the defined benefit plan, HSBC UK make contributions in accordance with advice from actuaries and in consultation with the plan's trustees where relevant. Contributions are required when the section's assets are considered insufficient to cover the existing pension liabilities. Contributions are typically revised once every three years.

The defined benefit plan invests contributions in a range of investments designed to limit the risk of assets failing to meet the plan's liabilities. Any changes in expected returns from the investments may also change future contribution requirements. In pursuit of these long-term objectives, an overall target allocation of the defined benefit plan assets between asset classes is established. In addition, each permitted asset class has its own benchmarks, such as stock market or property valuation indices or liability characteristics.

The benchmarks are reviewed on a manager by manager basis at least once every three to five years and more frequently if required by circumstances. The process takes account of changes in the plan's liabilities. The most significant benchmark is the interest rate and inflation hedging programme and this was last reviewed during 2019. The assets are invested in a diverse range of assets to reduce any concentrations of risk.

In addition, during 2019, the defined benefit plan performed longevity swap transactions with The Prudential Insurance Company of America ('PICA') a subsidiary of Prudential Financial, Inc. and with Swiss Re. The arrangements provide long term protection to the defined benefit plan against costs resulting from pensioners or their dependants living longer than initially expected and cover approximately three-quarters of the pensioner liabilities (50% with PICA and 25% with Swiss Re).

Market risk

Overview

Market risk is the risk that movements in market factors, such as foreign exchange rates, interest rates and credit spreads, will reduce our income or the value of our portfolios. Exposure to market risk is separated into two portfolios.

- Trading portfolios
- Non-trading portfolios.

A summary of our current policies and practices regarding the management of market risk is set out below.

Where appropriate, we apply similar risk management policies and measurement techniques to both trading and non-trading portfolios. Our objective is to manage and control market risk exposures to optimise return on risk while maintaining a market profile consistent with our established risk appetite.

Market risk management

The nature of the hedging and risk mitigation strategies performed corresponds to the market risk management instruments available within each operating jurisdiction. These strategies range from the use of traditional market instruments, such as interest rate swaps,

to more sophisticated hedging strategies to address a combination of risk factors arising at portfolio level.

Market risk governance

(Audited)

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

The management of market risk is principally undertaken in Markets and BSM using risk limits allocated from the risk appetite, which is subject to the HSBC Group RMM approval. The level of limits set is based on the overall risk appetite for HSBC UK being cascaded down to the individual entities and the limits required for the individual desks to be able to execute their stated business strategy under the HSBC UK ring-fencing Exceptions Policy. Limits are set for portfolios, products and risk types, with market liquidity being a primary factor in determining the level of limits set. The market risk limits for HSBC UK are endorsed at HSBC UK RMM.

Global Risk is responsible for setting market risk management policies and measurement techniques and is responsible for measuring market risk exposures in accordance with the policies defined by Global Risk, and monitoring and reporting these exposures against the prescribed limits on a daily basis.

HSBC UK is required to assess the market risks arising on each product in its business and to transfer them to either its local Markets unit for management, to balance sheet management books or to separate books managed under the supervision of ALCO.

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

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

The control of market risk in the trading and non-trading portfolios is based on a policy restricting individual operations to trading within a list of permissible instruments authorised for HSBC UK by Global Risk, enforcing new product approval procedures, and ensuring compliance with the HSBC UK Exceptions Policy implemented to ensure HSBC UK activity is compliant with the legislative restriction on ring fenced bodies.

Market risk measures

Monitoring and limiting market risk exposures

Our objective is to manage and control market risk exposures while maintaining a market profile consistent with HSBC UK strategy and risk appetite as well as operating within the HSBC Group's risk appetite for the entity. We use a range of tools to monitor and limit market risk exposures including sensitivity analysis, value at risk ('VaR'), and stress testing.

Sensitivity analysis

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

Value at risk ('VaR')

VaR is a technique that estimates the potential losses on risk positions as a result of movements in market rates and prices over a specified time horizon and to a given level of confidence. The use of VaR is integrated into market risk management and is calculated for all trading positions. HSBC UK does not have a market risk internal model approval and therefore VaR is not used for any regulatory return but only used for internal management information purposes. We use the standardised approach for its market risk capital calculation.

In addition, we calculate VaR for non-trading portfolios in order to have a complete picture of risk.

Stress testing

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

Stress testing is implemented at legal entity, regional and overall Group levels. Scenarios are tailored to capture the relevant events or market movements at each level. The risk appetite around potential stress losses is set and monitored against referral limits.

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

Stressed VaR and stress testing, together with reverse stress testing provides management with insights regarding the 'tail risk' beyond VaR for which appetite is limited.

Trading portfolios

Back-testing

Trading book VaR is not used for calculating capital requirements arising from market risk within HSBC UK therefore there is no back testing of trading book VaR.

Non-trading portfolios

Non-trading VaR of HSBC UK includes the interest rate risk of non-trading financial instruments held by the global businesses and transferred into portfolios managed by BSM or Asset Liability and Capital Management ('ALCM') functions. In measuring, monitoring and managing risk in our non-trading portfolios, VaR is just one of the tools used. The management of interest rate risk in the banking book is described further in 'Interest rate risk in the banking book' section below, including the role of BSM.

Our control of market risk in the non-trading portfolios is based on transferring the assessed market risk of assets and liabilities created outside BSM or Markets, to the books managed by BSM, provided the market risk can be neutralised. The net exposure is typically managed by BSM through the use of fixed rate government bonds (high quality asset held in held-to-collect-and sell (HTCS books)) and interest rate swaps. The interest rate risk arising from fixed rate government bonds held within HTCS portfolios is reflected within non-trading VaR. Interest rate swaps used by BSM are typically classified as either a fair value hedge or a cash flow hedge and included within non-trading VaR. Any market risk that cannot be neutralised in the market is managed by HSBC UK ALCM in segregated ALCO books.

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 does not have investments in subsidiaries in non-sterling currencies.

Interest rate risk in the banking book

Overview

Interest Rate Risk in the Banking Book ('IRRBB') is the risk of an adverse impact to earnings or capital due to changes in market interest rates. IRRBB is principally generated by our non-traded assets and liabilities. This risk is monitored and controlled by ALCM. Interest rate risk in the banking book is transferred to and managed by Balance Sheet Management ('BSM'), and also monitored by Wholesale Market Risk, Product Control and ALCM function with reference to established risk appetites.

Governance and structure

ALCM monitors and controls non-traded interest rate risk. This includes reviewing and challenging the business prior to the release of new products and in respect of proposed behavioural assumptions used for hedging activities. ALCM is also responsible for maintaining and updating the transfer pricing framework, informing the ALCO of the overall IRRBB exposure and managing the balance sheet in conjunction with BSM.

BSM manages the banking book interest rate positions transferred to it within the market risk limits approved by RMM. Effective governance of BSM is supported by the dual reporting lines it has to the Chief Executive Officer of GB&M and to the Group Treasurer, with Risk acting as a second line of defence. The global businesses can only transfer non-trading assets and liabilities to BSM provided BSM can economically hedge the risk it receives. Hedging is generally executed through interest rate derivatives or fixed-rate government bonds. Any interest rate risk that BSM cannot economically hedge is not transferred and will remain within the global business where the risks originate.

Measurement of interest rate risk in the banking book

The ALCM function uses a number of measures to monitor and control interest rate risk in the banking book, including:

- Non-traded VaR;
- Net Interest Income ('NII') sensitivity; and
- Economic value of equity ('EVE').

Non-traded VaR

Non-traded VaR uses the same models as those used in the trading book and excludes both HSBC Holdings and the elements of risk that are not transferred to BSM.

Net interest income sensitivity

A principal part of our management of non-traded interest rate risk is to monitor the sensitivity of expected net interest income ('NII') under varying interest rate scenarios (i.e. simulation modelling), where all other economic variables are held constant. This monitoring is undertaken by ALCO, where both one-year and five-year net interest income sensitivities across a range of interest rate scenarios are forecast.

Projected net interest income sensitivity figures represent the effect of pro forma movements in projected yield curves based on a static balance sheet size and structure. The exception to this is where the size of the balances or repricing is deemed interest rate sensitive, for example, non-interest-bearing current account migration and fixed-rate loan early prepayment. These sensitivity calculations do not incorporate actions that would be taken by BSM or in the business units to mitigate the effect of interest rate movements.

The net interest income sensitivity calculations assume that interest rates of all maturities move by the same amount in the 'up-shock' scenario. Rates are not assumed to become negative in the 'down-shock' scenario unless the central bank rate is already negative. In these cases, rates are not assumed to go further negative, which may, in certain currencies, effectively result in non-parallel shock. In addition, the net interest income sensitivity calculations take account of the effect of anticipated differences in changes between interbank and internally determined interest rates, where the entity has discretion in terms of the timing and extent of rate changes.

Economic value of equity

Economic value of equity ('EVE') represents the present value of the future banking book cash flows that could be distributed to equity providers under a managed run-off scenario. This equates to the current book value of equity plus the present value of future net interest income in this scenario. EVE can be used to assess the economic capital required to support interest rate risk in the banking book. 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. Operating entities are required to monitor EVE sensitivity as a percentage of capital resources.

Defined benefit pension scheme

Market risk also arises within HSBC UK's defined benefit pension plan to the extent that the obligations of the plan are not fully matched by assets with determinable cash flows. Refer to Pension risk section on page 46 for additional information.

Market risk in 2019

There were no material changes to our policies and practices for the management of market risk in 2019.

Exposure to market risk is separated into two portfolios.

Trading portfolios comprise positions arising from market-making and hedging of customer-derived positions or short dated trades executed for nostro management or liquidity management purposes.

Non-trading portfolios including BSM comprise positions that primarily arise from the interest rate management of the group's retail and commercial banking assets and liabilities and financial investments designated as held-to-collect-and-sale ('HTCS') held as part of the entities liquid asset buffer ('LAB').

Trading portfolios

(Audited)

The HSBC Group's preferred method of market risk capital calculations is to use a VaR model. However due to the small size of the regulatory trading portfolio within HSBC UK, the current approach to capital calculations for market risk in the trading portfolio within the group is to use the standardised model. Trading portfolio market risk exposures within the group are not material as customer facing trades within markets are hedged on a one for one basis and the BSM trading portfolio limits are primarily used for short-term cash management.

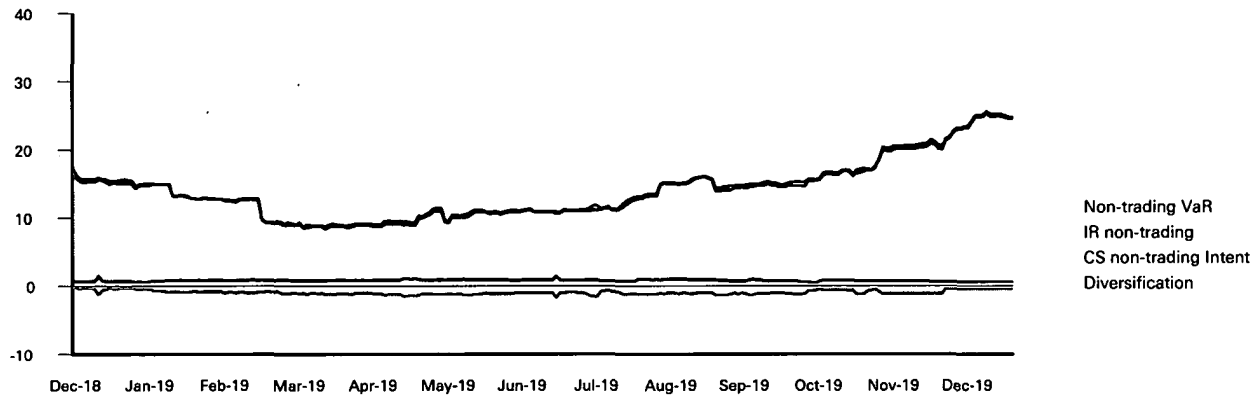
Value at Risk of the non-trading portfolios

(Audited)

Non-trading VaR of the group includes contributions from BSM and ALCO. It is primarily driven by interest rate risk of non-trading BSM positions which have the most significant market risk limits within HSBC UK. These limits and corresponding exposures are the consequence of BSM needing to meet its twin objectives of managing the structural interest rate risk transferred from the global businesses and the management of the entity's LAB. The daily levels of total non-trading VaR over the last year are set out in the graph below. The primary driver of the non-trading VaR is the Interest Rate risk exposure held within BSM (£24.5m IR VaR as at 31 December 2019). The main contributor of Interest rate risk within BSM are the securities held within the LAB and their corresponding hedges.

At the start of 2019, a proportion of the HTCS portfolio was converted from outright holdings to Asset Swaps reducing the outright interest rate risk duration on the book which brought about a reduction in the banking book VaR. Throughout the whole of 2019, the HSBC UK BSM desk looked to increase the diversity of the HSBC UK LAB by reducing the balance held in cash and central bank deposits and increasing the securities portion. The securities portion of the LAB was increased via the purchase of outright securities and asset swaps across USD, GBP and EUR, which increased both the outright interest rate risk and the treasury/non treasury basis risk. This increased the VaR of the non-trading portfolio.

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



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

Non-trading VaR, 99% 1 day

(Audited)

	Credit spread	Interest Rates	Diversification[1]	Total[2]
	£m	£m	£m	£m
Balance at 31 Dec 2019	**0.6**	**24.5**	**(0.4)**	**24.7**
Average	**0.8**	**14.1**	**(0.9)**	**13.9**
Maximum	**1.5**	**25.3**		**25.5**
Minimum	**0.5**	**8.7**		**8.4**
Balance at 31 Dec 2018	0.7	16.8	(0.2)	17.3
Average	1.1	20.7	(0.9)	20.9
Maximum	3.2	23.8		24.1
Minimum	0.6	16.7		17.0

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

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

Resilience risk

Overview

Resilience risk is the risk that we are unable to provide critical services to our customers, affiliates and counterparties, as a result of sustained and significant operational disruption. Sustained and significant operational disruption means events that affect:

- the stability of the financial system;
- the viability of the bank and our industry peers; or
- the ability of our customers to access our services.

We seek to understand the effects and outcomes of these events, prioritising services which are both vulnerable to disturbance and critical to our customer service offering.

Resilience risk management

Operational resilience is our ability to adapt operations to continue functioning when an operational disturbance occurs. We measure resilience in terms of the maximum disruption period or the impact tolerance that we are willing to accept for a business service.

Resilience risk cannot be managed down to zero, so we concentrate on critical business services that have the highest potential to threaten our ability to provide continued service to our customers. Our resilience strategy is focused on the establishment of robust back-up plans, detailed response methods, alternative delivery channels and recovery options.

The Resilience Risk team provides guidance and stewardship to our businesses and global functions about how we can prevent, adapt, and learn from resilience-related threats when something goes wrong. We view resilience through six lenses: strategic change and emerging threats, third-party risk, information and data resilience, payments and processing resilience, systems and cyber resilience, and protective security risk. IT Resilience (including Cyber) and Third Party Risk Management continue to be areas of particular focus for HSBC UK. These have developed significantly in 2019, and we will continue that focus and investment in 2020.

Key developments in 2019

In May 2019, we launched the Non-financial risk simplified risk taxonomy, which contained the new resilience risk. The new resilience risk brings together a number of existing risks such as cyber, ISR and Third Party Risk Management under one risk category.

Resilience risk was formed to simplify the way we interact with our stakeholders and to deliver clear, consistent and credible responses globally. Since that time, we have undertaken a number of initiatives to develop and embed the new sub-function and drive the management of resilience risk. These included:

- Development of a Target Operating Model to envision our desired state for the resilience risk function.
- Definition of the first line of defence responsibility for managing operational continuity and resilience within HSBC UK.
- Re-organisation of the second line of defence into a simplified resilience risk engagement model that eliminates duplication and ensures a coordinated response across the risk types.
- Recruitment of a new HSBC UK Head of Resilience Risk, who will commence duties in first quarter of 2020, providing challenge to the control owners of the key component areas of operational resilience.
- Enhancement of our risk oversight for the UK by strengthening the interlock between our Global functions/Business control committees, which includes Third Party and outsourcing.
- Establishment of the UK Service Governance oversight committee which aims to spotlight UK vulnerable services and protect them.
- Definition of the UK IT strategy, which has set a direction of travel to reduce complexity through simplification.

- Investment of significant resource and funds into improving how we understand and manage our engagements with Third Parties.

Governance and structure

The Group Resilience Risk Executive Committee ('RR ExCo') oversees resilience risk, and has accountability to Global Risk Management Board. The RR ExCo is supported by its sub-committees that provide oversight over each of the respective RR sub-teams.

The Resilience Risk Group Governance Meeting ensures that resilience risk is managed within its defined risk appetite. It is jointly chaired by the Global Head of Operational Resilience and the Group CIO. The Resilience Risk Group Governance Meeting has accountability into the Non-Financial Risk Management Board and is escalated (via individual accountability) to the Global Risk Committee.

Within the UK, resilience risk is managed within the HSBC UK RMM and Risk Committee, with clear escalation path into the RR EXCO and GRMM.

Key risk management process

The newly formed resilience risk team oversees the identification, management and control of resilience risks. Global policies and procedures are currently being re-written to align with the new resilience risk service catalogue. Within HSBC UK, we have undertaken a number of specific initiatives to develop and embed the new sub-function.

These include:

- Defining the first line of defence responsibility for managing operational continuity and resilience within HSBC UK.
- Re-organising the second line of defence into a simplified resilience risk engagement model that eliminates duplication and ensures a coordinated response across the disciplines.
- Undertaking recruitment of a new HSBC UK Head of Resilience Risk, who will commence duties in 1Q20, providing challenge to the control owners of the key component areas of operational resilience.

Regulatory compliance risk management

Overview

Regulatory compliance risk is the risk that we fail to observe the letter and spirit of all relevant laws, codes, rules, regulations and standards of good market practice, and as a consequence incur fines and penalties and suffer damage to our business.

Regulatory compliance risk arises from the risks associated with breaching our duty to our customers and other counterparties, inappropriate market conduct and breaching other regulatory requirements.

Regulatory developments

Financial service providers continue to operate to stringent regulatory and supervisory requirements, particularly in the areas of capital and liquidity management, conduct of business, financial crime, internal control frameworks, the use of models and the integrity of financial services delivery.

Key elements of the regulatory agenda in 2019 have focussed on the introduction of 'Open Banking' technologies, fair pricing in financial services and additional High Cost Credit remedies including overdrafts. Looking forward to 2020, we expect further developments in relation to proposals designed to enhance consumer protection, treatment of vulnerable customers as well as further work on operational resilience. Consideration is now being given to the Future of Financial Services Regulation as the UK exits the European Union. HMT's Future Regulatory Framework (FRF) review commenced in late 2019 and is expected to continue in 2020, the outcome of which may result in refinements to the regulatory framework.

As a result of the UK's decision to leave the EU, the FCA, PRA and HMT have progressed necessary actions to ensure that EU laws and regulations that are directly applicable to UK firms were transposed into UK law and regulation ahead of the 31st of January, the official date of exit. A transition period for the UK and EU to negotiate a future relationship is now in place until the 31 December 2020, during which EU rights and obligations continue to apply. A series of statutory instruments and changes to the FCA and PRA Handbooks to onshore EU law and regulation have been published. In the absence of an agreement on the future relationship, such transposed laws will take effect at the end of the transition period.

We continue to engage in the development of new and amended regulations in the UK to ensure that the implications have been fully considered by regulators and the wider industry.

We will continue to work with the UK Authorities and Regulatory Bodies to discuss contingency and scenario planning throughout the transition period.

Conduct of business

Financial institutions continue to operate under increased level of scrutiny regarding conduct of business, particularly in relation to fair outcomes for customers, especially those in vulnerable positions, and orderly and transparent operations in financial markets. Key stakeholders, including regulators, prosecutors, the media and the public have heightened expectations as to the behaviour and conduct of financial service providers, and any shortcomings or failure to demonstrate adequate controls are in place to mitigate such risks could result in regulatory sanctions, fines or an increase in civil litigation.

A number of thematic areas were identified as priorities for UK Regulatory Compliance in 2019, taking into account our regulators' expectations, key business risks, and other known activities and initiatives. These included areas such as product governance, customer redress initiatives and vulnerable customers.

We further enhanced the way our operational risk management framework facilitates the delivery of fair outcomes for customers, and to maintain financial market integrity.

Financial crime and fraud risk management

Overview

Financial crime and fraud risk is the risk that we knowingly or unknowingly help parties to commit or to further potentially illegal activity. Financial crime risk arises from day-to-day banking operations.

Key developments in 2019

During 2019, HSBC UK continued to increase efforts to strengthen its ability to combat financial crime. HSBC UK integrated into day-to-day operations the majority of the financial crime risk core capabilities delivered through the Global Standards programme, which was set up in 2013 to enhance risk management policies, processes and systems. The HSBC Group has begun several initiatives to define the next phase of financial crime risk management which are applicable to HSBC UK.

- Continued strengthening of anti-fraud capabilities, focusing on threats posed by new and existing technologies, and delivery of a comprehensive fraud training programme to our people.
- Continued investment in the use of artificial intelligence ('AI') and advanced analytics techniques to develop a financial crime risk management framework for the future.
- Advanced anti-money laundering ('AML') and sanctions automation systems were launched to detect and disrupt financial crime in international trade. These systems will help strengthen our ability to fight financial crime through the detection of suspicious activity and possible criminal networks.

Governance and structure

HSBC UK has continued to strengthen and review the effectiveness of our governance framework to manage financial crime and fraud risk. Formal governance committees are held across HSBC UK, enabling compliance with the letter and the spirit of all applicable financial crime compliance laws and

regulations, and the Group's own standards, values and policies relating to financial crime risks.

In 2019, the HSBC UK Board has received regular reports from the HSBC UK Head of Financial Crime Compliance on actions being taken to address issues and vulnerabilities in relation to financial crime and updates on the ongoing work to strengthen financial crime controls.

Key risk management processes

HSBC UK continued to deliver a programme to further enhance the policies and controls around identifying and managing the risks of bribery and corruption across the business. A Group transformation programme, applicable to HSBC UK, also continues to strengthen anti-fraud capabilities, and strengthen anti-tax evasion controls. The Group and HSBC UK have strengthened governance and policy frameworks and improved the management information reporting process which demonstrates the effectiveness of our financial crime controls. The Group continue to invest in the next generation of capabilities to fight financial crime by applying advanced analytics and artificial intelligence. HSBC UK remains committed to enhancing our risk assessment capabilities, and to delivering more proactive risk management.

Working in partnership with the public and private sector is vital to managing financial crime risk. HSBC UK are strong proponents of public-private partnerships and information-sharing initiatives. During 2019, HSBC UK continued to work in partnership with the Joint Money Laundering Intelligence Taskforce, in order to bring further benefit to the bank by enhancing the understanding of financial crime risks through information sharing and support economic crime reform through work with the UK Economic Crime Strategic Board, the UK government and UK law enforcement agencies.

Skilled person/Independent consultant

Following expiration in December 2017 of the anti-money laundering Deferred Prosecution Agreement entered into with the US Department of Justice ('DoJ'), the then Monitor has continued to work in his capacity as a Skilled Person under Section 166 of the Financial Services and Markets Act under the Direction issued by the UK Financial Conduct Authority ('FCA') in 2012. He has also continued to work in his capacity as an Independent Consultant under a cease-and-desist order issued by the US Federal Reserve Board ('FRB'). This work is applicable to the HSBC UK.

The Skilled Person has assessed the progress of the HSBC Group towards being able to effectively manage its financial crime risk on a business-as-usual basis. As part of this review, the Skilled Person has undertaken a review of HSBC UK and has noted that HSBC UK continues to make material progress towards its financial crime risk target end state in terms of key systems, processes and people. Nonetheless, the Skilled Person has identified some areas that require further work before HSBC UK reaches a business-as-usual state. We recognise that there is more to do before our financial crime compliance programme is fully operationally effective. Reflective of the HSBC Group's significant progress in strengthening its financial crime risk management capabilities, the HSBC Group's engagement with the current Skilled Person will be terminated and a new Skilled Person with a narrower mandate will be appointed to assess the remaining areas that require further work in order for the HSBC Group, including HSBC UK, to transition fully to business-as-usual financial crime risk management. The FCA also intends to take steps to maintain global oversight of the HSBC Group's management of financial crime risk.

The Independent Consultant completed his sixth annual assessment, which was primarily focused on HSBC's sanctions programme and included HSBC UK. The Independent Consultant concluded that the HSBC Group and HSBC UK continue to make significant strides toward establishing an effective sanctions compliance programme, commending the Group's material progress since the fifth annual assessment in 2018. The Independent Consultant has, however, determined that certain areas within the Group's sanctions compliance programme require further work. A seventh annual assessment will take place in the first quarter of 2020. The Independent Consultant will continue to carry out an annual Office of Foreign Assets Control compliance review, at the FRB's discretion.

Model risk

Overview

Model risk is the potential for adverse consequences from business decisions informed by models, which can be exacerbated by errors in methodology, design or the way they are used. Model risk arises in both financial and non-financial contexts whenever business decision making includes reliance on models.

Key developments in 2019

In 2019 we carried out a number of initiatives to further develop and embed the Model Risk Management, including:

- Investing in the HSBC UK Model Risk Management Function.
- We refined the model risk policy to enable a more risk-based approach to model risk management.
- We designed a new target operating model for Model Risk Management, informed by internal and industry best practice. This will drive the evolution of the overall governance framework to ensure best practice.
- We are refreshing the existing model risk controls to enable better understanding of control objectives and to provide the modelling areas with implementation guidance to enhance effectiveness.

Governance and structure

HSBC UK has a Head of Model Risk Management who reports into the HSBC UK CRO.

Key risk management processes

Global responsibility is delegated from the Risk Management Meeting of the Board to the Global Model Risk Committee, which is chaired by the Group Chief Risk Officer. This committee regularly reviews our Global model risk management policies and procedures that HSBC UK complies with, and requires the first line of defence to demonstrate comprehensive and effective controls based on a library of model risk controls provided by Model Risk Management. HSBC UK has a Model Risk Committee that escalates locally via the HSBC UK RMM and also globally via the Global Model Risk Committee.

Model Risk Management also report on model risk to senior management on a regular basis through the use of the risk map and top and emerging risks.

We regularly review the effectiveness of these processes, including the model oversight committee structure, to ensure appropriate understanding and ownership of model risk is embedded in the businesses and functions.

Capital

Capital overview

Key capital numbers

	Footnotes	At 31 Dec 2019	2018
Available capital (£m)	1		
Common equity tier 1 capital		**11,202**	11,700
Tier 1 capital		**13,453**	13,896
Total regulatory capital		**16,462**	16,826
Risk-weighted assets (£m)			
Credit risk	2	**75,353**	81,135
Counterparty credit risk		**198**	66
Market risk		**27**	38
Operational risk		**10,303**	10,600
Total risk-weighted assets		**85,881**	91,839
Capital ratios (%)			
Common equity tier 1		**13.0**	12.7
Total tier 1		**15.7**	15.1
Total capital		**19.2**	18.3
Leverage ratio			
Total leverage ratio exposure measure (£m)		**268,271**	246,659
Leverage ratio (%)		**5.0**	5.6

1 *Unless otherwise stated, all figures are calculated using the EU's regulatory transitional arrangements for IFRS 9 'Financial Instruments' in article 473a of the Capital Requirements Regulation.*
2 *'Credit risk' here, and in all tables where the term is used, excludes counterparty credit risk.*

Capital management

Approach and policy

(Audited)

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

We manage group capital to ensure that we exceed current and expected future requirements. Throughout 2019, we complied with the PRAs regulatory capital adequacy requirements, including those relating to stress testing.

Capital measurement

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

Our policy and practice in capital measurement and allocation at the group level is underpinned by the Capital Requirements Regulation and the Capital Requirements Directive ('CRD IV') rules and any national discretions applied by the PRA.

The Basel III framework is structured around three 'pillars': minimum capital requirements, supervisory review process and market discipline. Basel III introduced a number of capital buffers, including the Capital Conservation Buffer, Countercyclical Capital Buffer and other systemic risk buffers. CRD IV legislation implemented Basel III in the EU, and the 'PRA Rulebook' for CRR Firms transposed the various national discretions under the CRD IV legislation into UK requirements.

The Bank of England announced Systemic Risk Buffer ('SRB') rates for the UK Ring-Fenced banks applicable from 1 August 2019. These are set as a percentage of the risk-weighted assets, with HSBC UK subject to a SRB of 1% of total RWAs at the sub-consolidated level. These rates are refreshed annually.

Regulatory capital

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

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

Risks to capital

Outside the stress testing framework, 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.

In June 2017, the PRA published its final policy statement setting out revisions to the way that firms model probability of default ('PD') and loss given default ('LGD') for residential mortgage exposures, in order to mitigate cyclicality. In addition,the PRA also removed the discretion to use 180 days instead of 90 days in the 'days past due' component of the definition of default for exposures secured by residential mortgages, and certain small and medium sized enterprise (SME) commercial mortgages. These changes will need to be implemented by the end of 2020.

In December 2017, the Basel Committee on Banking Supervision ('Basel') published the Basel III Reforms. The package aims for a 1 January 2022 implementation, with a five-year transitional provision for the output floor. This floor ensures that, at the end of the transitional period, banks' total RWAs are no lower than 72.5% of those generated by the standardised approaches. The final standards will need to be transposed into the relevant local law before coming into effect.

We continue to evaluate the final package. Given that the package contains a significant number of national discretions, the possible impact is uncertain.

Own funds

Own funds disclosure

(Audited) Ref*		At 31 Dec 2019 £m	31 Dec 2018 £m
	Common equity tier 1 (CET1) capital: instruments and reserves		
1	Capital instruments and the related share premium accounts	**9,015**	9,015
	– ordinary shares	**9,015**	9,015
2	Retained earnings	**10,978**	10,713
3	Accumulated other comprehensive income (and other reserves)	**(211)**	(399)
5a	Independently reviewed interim net profits net of any foreseeable charge or dividend	**161**	562
6	**Common equity tier 1 capital before regulatory adjustments**	**19,943**	19,891
28	Total regulatory adjustments to common equity tier 1	**(8,741)**	(8,191)
29	**Common equity tier 1 capital**	**11,202**	11,700
36	Additional tier 1 capital before regulatory adjustments	**2,251**	2,196
44	**Additional tier 1 capital**	**2,251**	2,196
45	**Tier 1 Capital (T1 = CET1 + AT1)**	**13,453**	13,896
51	Tier 2 capital before regulatory adjustments	**3,009**	2,930
58	**Tier 2 capital**	**3,009**	2,930
59	**Total capital**	**16,462**	16,826

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

Throughout 2019, we complied with the PRA's regulatory capital adequacy requirements.

At 31 December 2019, our common equity tier 1 ('CET1') ratio increased to 13.0% from 12.7% at 31 December 2018 as a result of a reduction in RWAs.

CET1 capital decreased during the year by £0.5bn, mainly due to a rise in the deduction for excess expected loss.

Our Pillar 2A requirement at 31 December 2019, as per the PRA's Individual Capital Requirement based on a point-in-time assessment, was 4.19% of RWAs, of which 2.35% was met by CET1.

Risk-weighted assets

RWAs decreased by £6.0bn in the year, mainly from Internal model and methodology updates (£7.5bn) and new or updated models (£1.2bn), partially offset by the effects of an increase in book size (£2.4bn) and an external policy update (£0.3bn).

Methodology and policy

RWAs reduced following the implementation of a number of initiatives during the year:

- PRA approval of a change in the calculation of RWAs for defaulted clients (£3.5bn), which was partly offset by an increase in Expected Loss.
- The implementation of a new securitisation programme resulted in a reduction to RWAs of £1.0bn.
- Review and update of customer data, notably Customer Risk Rating and LGD amendments (£2.6bn)

RWAs increased by £0.3bn as a result of a change in the accounting treatment of leased assets.

Model updates

RWAs in CMB decreased following PRA approval of an update to the large corporate model, and decreased in RBWM following approval by the PRA of new models in first direct for current accounts, credit cards and personal loans.

Asset size

CMB RWAs increased due to growth in Corporate lending. RBWM RWAs rose primarily due to increased mortgage lending.

On 1 January 2020, exposures subject to the UK corporate loss-given-default model moved from the advanced to the foundation approach.

RWA movement by business by key driver

	Credit risk, counterparty credit risk and operational risk						
	RBWM £m	CMB £m	GB&M £m	GPB £m	Corporate Centre £m	Market risk £m	Total RWAs £m
RWAs at 1 Jan 2019	**21,370**	**66,009**	**22**	**1,924**	**2,476**	**38**	**91,839**
Transfers	–	(230)	–	–	–	–	(230)
Asset size	785	1,688	262	(29)	(326)	(9)	2,371
Asset quality	719	(177)	–	(167)	(110)	–	265
Model updates	(472)	(687)	–	–	–	–	(1,159)
– portfolios moving onto IRB approach	–	–	–	–	–	–	–
– new/updated models	(472)	(687)	–	–	–	–	(1,159)
Methodology and policy	(334)	(6,924)	54	65	(59)	–	(7,198)
– internal updates	(334)	(6,924)	54	65	(398)	–	(7,537)
– external updates – regulatory	–	–	–	–	339	–	339
Foreign exchange movement	–	–	(1)	–	(4)	(2)	(7)
Total RWA movement	**698**	**(6,330)**	**315**	**(131)**	**(499)**	**(11)**	**(5,958)**
RWAs at 31 Dec 2019	**22,068**	**59,679**	**337**	**1,793**	**1,977**	**27**	**85,881**

Leverage ratio

Our leverage ratio, calculated in accordance with the Capital Requirements Regulation, was 5.0% at 31 December 2019, down from 5.6% at 31 December 2018.

The decrease in the ratio was largely due to growth in the balance sheet.

Pillar 3 disclosure requirements

Pillar 3 of the Basel regulatory framework is related to market discipline and aims to make financial services firms more transparent by requiring publication of wide-ranging information on their risks, capital and management. Our *Pillar 3 Disclosures at 31 December 2019* is published on HSBC Group's website, www.hsbc.com, under 'Investors'.

Corporate governance report

The statement of corporate governance practices set out on pages 54 to 59 and information incorporated by reference constitutes the corporate governance report of HSBC UK Bank plc.

Corporate governance statement

The bank is, together with the wider Group, committed to high standards of corporate governance. The Group has a comprehensive range of corporate governance principles, policies and procedures influenced by the UK Corporate Governance Code with requirements for subsidiaries in respect of Board independence, composition and effectiveness to ensure that the Group is well managed, with appropriate oversight and control. HSBC UK is also subject to robust corporate governance requirements imposed by the PRA's Ring-Fenced Bodies Regulations. These corporate governance requirements surpass those of the alternative governance codes. As such, the bank did not apply any specific corporate governance code during the financial year.

During the year, the bank complied with all of HSBC's corporate governance principles, policies and procedures and also with those in the PRA's Ring-Fenced Bodies Regulations.

The Directors serving as at 31 December 2019 are set out below.

Directors

Dame Clara Furse

Chairman and independent non-executive Director

Chairman of the Chairman's Nominations and Remuneration Committee.

Appointed to the Board: April 2017

Clara is a non-executive director of Vodafone Group plc and Amadeus IT Group, S.A. She is a member of the Panel of Senior Advisors to Chatham House and of Bocconi University's International Advisory Council. Former appointments include: external member of the Bank of England's Financial Policy Committee; lead independent director of the UK's Department for Work and Pensions; Chief Executive of the London Stock Exchange; Group Chief Executive of Credit Lyonnais Rouse; member of the Shanghai International Financial Advisory Council and non-executive director of Euroclear plc, LCH Clearnet Group Ltd., Fortis SA, Nomura Holdings and the Legal & General Group.

John David Stuart (known as Ian Stuart)

Executive Director and Chief Executive Officer

Chairman of the Executive Committee.

Appointed to the Board: May 2017

Ian joined the HSBC Group in 2014. He is a Group Managing Director of HSBC Holdings plc and a board member of UK Finance, the industry association for the financial services sector. He is also a business ambassador for Meningitis Now. Ian has worked in financial services for almost four decades. He joined HSBC as a Group General Manager and Head of Commercial Banking Europe in 2014, having previously led the corporate and banking businesses in Barclays and Natwest. He started his career at the Bank of Scotland.

Jonathan James Calladine (known as James Calladine)

Executive Director and Chief Risk Officer

Member of the Executive Committee.

Appointed to the Board: October 2017

James joined the HSBC Group in 1983. He took up the post of UK Chief Risk Officer and was appointed to the Board in October 2017. Former HSBC Group roles include: Chief Risk Officer for the HSBC Group's Latin American operations; regional Chief Risk Officer for Continental Europe; and Senior Manager, Internal Audit in Asia Pacific.

James Coyle

Independent non-executive Director

Chairman of the Audit Committee and a member of the Risk Committee and Chairman's Nominations and Remuneration Committee.

Appointed to the Board: May 2018

James is chairman of Marks & Spencer Unit Trust Management Limited and a non-executive director of Marks and Spencer Financial Services plc (together, M&S Bank) and a member of the Audit & Risk Committee of M&S Bank. James is also chairman of HSBC Trust Company (UK) Limited and a non-executive director and member of the Audit and Risk Committee of HSBC Private Bank (UK) Limited. He is a non-executive director and chairman of the Audit and Risk Committee of Scottish Water, a non-executive director and chairman of the Audit and Risk Committee of Honeycomb Investment Trust plc, and an independent non-executive member of Deloitte UK Oversight Board. Former appointments include: chairman and chairman of the Audit and Risk Committee of World First UK Limited; member of Committees of the Financial Reporting Council, Group Financial Controller for Lloyds Banking Group; Group Chief Accountant of Bank of Scotland; member of the Audit Committee of the British Bankers Association; non-executive director of the Scottish Building Society; and a non-executive director and chairman of the Audit Committee of Vocalink plc.

Mridul Hegde CB

Independent non-executive Director

Chairman of the Risk Committee and a member of the Audit Committee and the Chairman's Nominations and Remuneration Committee.

Appointed to the Board: February 2018

Mridul's former appointments include: non-executive Director of the UK Municipal Bonds Agency and member of its Risk and Audit Committee; and senior roles at the Financial Reporting Council and HM Treasury, where she was Director of Financial Stability during the 2008 financial crisis and prior to that, Director of Public Spending.

Dame Denise Holt

Independent non-executive Director

Member of the Audit Committee.

Appointed to the Board: May 2018

Denise is a non-executive director of Iberdrola SA and Chairs the Council of the University of Sussex and the Cañada Blanch Centre for Contemporary Spanish Studies at the London School of Economics. Former appointments include: chairman and non-executive director of Marks and Spencer Financial Services plc; a member of the Board of Governors at Nuffield Health; member of

the board of Ofqual (examinations regulators) and of the NHS pay review body. Her career in the Foreign & Commonwealth Office included 40 years' experience of working in government, with postings in Ireland, Brazil and, as a senior Ambassador, in Mexico and Spain.

Alan Keir

Non-executive Director

Member of the Audit Committee and Risk Committee.

Appointed to the Board: February 2018

Alan is a non-executive director of Sumitomo Mitsui Bank Europe and Majid Al Futtaim Holdings. He is Honorary President of Horizons, the Association for former HSBC employees. Former appointments include a variety of senior executive roles within the HSBC Group. He was a Group Managing Director of HSBC Holdings plc from 2011 until his retirement from the Group in March 2016. He has previously served on the boards of HSBC Bank plc, HSBC Turkey, HSBC Trinkaus and Burkhardt, HSBC Bank Middle East and HSBC France. He is also a former Board member of the British Bankers Association, the UK-UAE Business Council, the Private Sector Council for GREAT (a government campaign to promote the best of Great Britain) and the University of Bradford School of Management Advisory Board. He has also sat on the Advisory Council of TheCityUK.

Rosemary Leith

Independent non-executive Director

Member of the Risk Committee

Appointed to the Board: February 2018

Rosemary is a non-executive director of: YouGov plc where she chairs the Remuneration Committee and is also a member of the Audit Committee; and the World Wide Web Foundation. Rosemary is a Trustee of the National Gallery where she chairs the Digital Advisory Board and a member of the Advisory Councils of Glasswing Ventures, Motive Partners and the Queens University School of Business. She is a Fellow at Harvard University's Berkman Klein Centre. Former appointments include: director of the Almeida Theatre, member of the Advisory Board of Infinite Analytics and Oxford University Wolfson College, and chair of the Council on Cyber security for the World Economic Forum, Global Agenda Council.

David Lister

Independent non-executive Director

Member of the Audit Committee and Risk Committee.

Appointed to the Board: May 2018

David is a non-executive director and chairman of HSBC Private Bank (UK) Limited, Marks and Spencer Financial Services plc and FDM Group (Holdings) plc. He is also a non-executive director of Interxion Holding N.V.; and a member of the board of governors at Nuffield Health. Former appointments include: non-executive director of CIS General Insurance Limited, Weatherbys Limited and the Department for Work and Pensions; Trustee of The Tech Partnership Limited; and Group Chief Information Officer at each of National Grid, Royal Bank of Scotland, Reuters and Boots.

Philippe Leslie Van de Walle (known as Leslie Van de Walle)

Independent non-executive Director

Member of the Risk Committee and Chairman's Nominations and Remuneration Committee

Appointed to the Board: February 2018

Leslie is the senior independent director and chairman of the Remuneration Committee of DCC plc, non-executive chairman of Euromoney Institutional Investor plc and, until 24 March 2020, a non-executive director and deputy chairman of Crest Nicholson Holdings plc. Former appointments include: non-executive Chairman of Robert Walters plc, SIG plc and Weener Plastic Packaging Group; non-executive director of Cape plc and Aegis Group plc; non-executive director and member of the Risk Committee of Aviva plc; senior independent non-executive director and member of the Risk & Regulatory Committee and Remuneration Committee of La Seda de Barcelona; Group CEO of United Biscuits plc and Rexam plc; and Executive Vice President Global Retail and Chairman, Europe of Royal Dutch Shell plc.

David Watts

Executive Director and Chief Financial Officer

Member of the Executive Committee.

Appointed to the Board: October 2017

Dave joined the HSBC Group in 1994. He took up the post of UK Chief Financial Officer and was appointed to the Board in October 2017. Former HSBC Group roles include: Chief Financial Officer for: HSBC Bank plc, Global Commercial Banking, the Middle East and North Africa, Group HSBC Technology and Operations, Global Banking, and HSBC Securities (USA) Inc; Head of Group Cost and Investment Reporting & Analysis; and Manager Treasury Services, France.

Company Secretary

Nicola Black

Nicola joined the HSBC Group in 2000 and was appointed Company Secretary in May 2017. She previously served as Company Secretary of HSBC Bank plc (2014-2017) and prior to that as Assistant Group Company Secretary, HSBC Holdings plc.

Board of Directors

The role of the Board is to provide entrepreneurial leadership of the bank within a framework of prudent and effective controls which enables risks to be assessed and managed. The Board is collectively responsible for the long-term success of the bank and delivery of sustainable value to shareholders.

It reviews the strategy for the bank and approves the risk appetite statement, capital and operating plans presented by management.

The roles of the Chairman and Chief Executive Officer are separate: the Chairman leads the Board and is responsible for its effectiveness and the Chief Executive Officer leads the business and is responsible for executing the strategy.

The majority of Board members, including the Chairman, are independent.

The Board meets regularly and Directors receive information between meetings about developments in the group's business. All Directors have full and timely access to all relevant information and may take independent professional advice if necessary.

The names of Directors serving at the date of this report and brief biographical particulars for each of them are set out on pages 54 and 55.

All Directors, including those appointed by the Board to fill a casual vacancy, are subject to annual re-election at the bank's Annual General Meeting. Non-executive Directors have no service contracts.

How the Directors have regard to key stakeholders

As described on page 7, the Board considers feedback from engagement exercises with employees and key stakeholders throughout the year and has regard to the interest of these stakeholders when approving the risk appetite statement, capital and operating plans, resulting in more robust challenge of management's proposals and stronger plans to achieve the bank's strategic objectives. Details about how the Directors have engaged with employees and had regard to their interests and the need to foster the company's business relationships when making decisions can be found on page 7.

Directors' emoluments

Details of the emoluments of the Directors of the bank for 2019, disclosed in accordance with the Companies Act, are shown in Note 3 'Employee compensation and benefits'.

Board committees

The Board has established a number of committees to assist it in discharging its responsibilities, the membership of which comprises certain Directors and, where appropriate, senior executives. The Chairman of each non-executive Board committee reports to each meeting of the Board on the activities of the Committee since the previous Board meeting. All such committees are accountable to the Board.

All of the members of the Chairman's Nominations and Remuneration Committee and the majority of members of the Audit and Risk Committees are independent non-executive Directors.

As at the date of this report, the following are the principal committees:

Audit Committee

The Audit Committee has non-executive responsibility for oversight of and advice to the Board on financial reporting related matters, including relevant internal controls.

The Committee meets regularly with the bank's senior financial and internal audit management and the external auditor to consider, among other matters; the group's financial reporting; the nature and scope of audit reviews; the effectiveness of the systems of internal control relating to financial reporting; and ensuring that the Internal Audit function supports the ability of the bank to be able to take decisions independently of other members of the HSBC Group by having appropriate standing within the bank and being free from constraint by management or other restrictions.

The current members are: James Coyle (Chairman); Mridul Hegde, Denise Holt, Alan Keir and David Lister.

Risk Committee

The Risk Committee has been delegated responsibilities from the Board in relation to non-executive oversight of risk related matters and the enterprise risks impacting the group, risk governance and internal control systems (other than internal financial control systems).

The Committee holds regular meetings with the bank's senior financial, risk, internal audit and compliance management and the external auditor to discharge its delegated responsibilities including to consider, among other matters: current and forward-looking risk exposures; the group's risk appetite and tolerance for determining strategy; the alignment of remuneration with risk appetite; and ensuring that the risk management function supports the ability of the bank to take decisions independently of other members of the HSBC Group by having appropriate standing within the bank and being free from constraint by management or other restrictions.

The current members are: Mridul Hegde (Chairman); James Coyle; Alan Keir; David Lister; Rosemary Leith; and Leslie Van de Walle.

Chairman's Nominations and Remuneration Committee

The Chairman's Nominations and Remuneration Committee has responsibility for matters related to nomination and remuneration as delegated by the Board. It is responsible for: (i) leading the process for Board appointments and for identifying and nominating, for approval by the Board, candidates for appointment to the Board; (ii) the endorsement of certain board and senior executive appointments for the material subsidiaries of the bank; and (iii) reviewing the implementation and appropriateness of the Group's remuneration policy and the remuneration of the bank's senior executives. It also has responsibility for the oversight of the bank's whistleblowing arrangements.

In undertaking its responsibilities, the Committee shall, among other things, plan for the orderly succession of the Board; review the Board's structure, size and composition, including skills, knowledge and diversity of the Board; assess the independence of non-executive Directors by reference to the criteria in the ring-fencing rules; and ensure that remuneration policies, practices and procedures are in line with the business strategy, objectives, values and long-term interests of the Company.

The current members are: Dame Clara Furse (Chairman); James Coyle; Mridul Hegde; and Leslie Van de Walle.

Executive Committee

The Executive Committee meets regularly and operates as a general management committee under the direct authority of the Board, exercising all of the powers, authorities and discretions of the Board in so far as they concern the management and day-to-day running of the bank, in accordance with such policies and directions as the Board may from time to time determine. The bank's Chief Executive Officer, Ian Stuart, chairs the Committee.

Regular Risk Management Meetings of the Executive Committee, chaired by the Chief Risk Officer, are held to establish, maintain and periodically review the policy and guidelines for the management of risk within the group.

Regular Financial Crime Risk Management meetings of the Executive Committee, chaired by the Chief Executive Officer, are held to ensure effective enterprise wide management of financial crime risk within the group and to support the Chief Executive Officer in discharging his financial crime risk responsibilities.

Post balance sheet events

Details on post balance sheet events can be found in note 28 to the financial statements.

Likely future developments

Details on the likely future developments in the business can be found in the 'future focus' sections on pages 4 and 5.

Companies (Miscellaneous Reporting) Regulations 2018

With the exception of the statement regarding corporate governance arrangements, the disclosures required under these regulations can be found in the section 172 statement set out in the Strategic Report.

Dividends

Information about dividends is provided on page 15 of the Strategic Report.

Internal control

The Board is responsible for the Risk Appetite Statement and any risk within the Risk Appetite Statement outside of risk tolerance. This is discharged through reviewing the effectiveness of risk management and internal control systems and for determining the aggregate level and types of risks the bank is willing to take to achieve its strategic objectives.

The bank has policies in place to ensure compliance with the PRAs Rulebook for Ring-fenced bodies, including an over-arching Ring-fenced bodies policy, together with additional policies covering Exceptions, Arm's Length Transactions and Distributions.

In addition, the group has implemented procedures designed to safeguard assets against unauthorised use or disposal, maintain proper accounting records and ensure the reliability and usefulness of financial information whether used within the business or for publication.

These procedures can only provide reasonable assurance against material mis-statement, errors, losses or fraud. They are designed

to provide effective internal control within the bank. The procedures have been in place throughout the year and up to 17 February 2020, the date of approval of the *Annual Report and Accounts 2019*.

Key risk management and internal control procedures include the following:

- The Group's Global Principles set an overarching standard for all other policies and procedures and are fundamental to the Group's risk management structure. They inform and connect our purpose, values, strategy and risk management principles, guiding us to do the right thing and treat our customers and our colleagues fairly at all times.
- Appointments to the most senior positions within the bank require the endorsement of the Board of Directors of HSBC Holdings plc.
- Delegation of authority within limits set by the Board. Authority to manage the day to day running of the bank is delegated within limits set by the Board to the Chief Executive Officer who has responsibility for overseeing the establishment and maintenance of systems of control appropriate to the business and authority to delegate such duties and responsibilities as he sees fit.
- Risk identification and monitoring. Systems and procedures are in place to identify, measure, monitor, control and report on the material risk types facing the group.
- Changes in market conditions/practices. Processes are in place to identify new risks arising from changes in market conditions/ practices or customer behaviours, which could expose the group to heightened risk of loss or reputational damage. The group employs a top and emerging risks framework which enables it to identify current and forward-looking risks and to take action which either prevents them materialising or limits their impact.
- Responsibility for risk management. All employees are responsible for identifying and managing risk within the scope of their role as part of the three lines of defence model, which is an activity-based model to delineate management accountabilities and responsibilities for risk management and the control environment. The second line of defence sets the policy and guidelines for managing specific areas, provides advice and guidance in relation to the risk, and challenges the first line of defence (the risk owners) on effective risk management.
- Strategic plans. Strategic plans are prepared annually for each of the businesses that make up the group, within the framework of the HSBC Group's overall strategy. These business strategic plans are brought together into the five year HSBC UK Country Strategic Plan, which is refreshed every three years. Progress against the Country Strategic Plan is reported regularly to the Executive Committee, Board and the HSBC Group Management Board. The bank also approves a financial Annual Operating Plan, which is informed by detailed analysis of risk appetite, describing the types and quantum of risk that the bank is prepared to take in executing its strategy and sets out the key business initiatives and the likely financial effects of those initiatives.
- IT operations. Centralised control is exercised over all IT developments and operations. Common systems are employed for similar business processes wherever practicable.

The key risk management and internal control procedures over financial reporting include the following:

- Audit Committee. The Audit Committee reviews financial reporting disclosures made by the bank for any material errors, misstatements or omissions. The integrity of disclosures is underpinned by structures and processes within the group's Finance and Risk functions that support rigorous analytical review of financial reporting and the maintenance of proper accounting records.
- Financial reporting. The bank's financial reporting process for preparing the consolidated *Annual Report and Accounts 2019* is controlled using documented accounting policies and reporting formats, supported by detailed instructions and guidance on reporting requirements, issued by the HSBC Group to HSBC UK that are then cascaded to all reporting entities within the group in advance of each reporting period end. The submission of the bank's financial information is subject to certification by the responsible financial officer, and analytical review procedures at reporting entity and group levels.
- Subsidiary certifications. Full and half-yearly certifications are provided to the Audit Committee and the Risk Committee from audit and risk committees of principal subsidiary companies, confirming that their financial statements have been prepared in accordance with Group policies, presented fairly the state of affairs of the relevant principal subsidiary and are prepared on a going concern basis.

During the year, the Risk Committee and the Audit Committee have kept under review the effectiveness of this system of internal control and have reported regularly to the Board. In carrying out their reviews, the Audit Committee and Risk Committee receive regular business and operational risk assessments; regular reports from the heads of key risk functions, which cover all internal controls, both financial and non-financial; internal audit reports; external audit reports; prudential reviews; and regulatory reports.

The Risk Committee monitors the status of principal risks and considers whether the mitigating actions put in place are appropriate. In addition, when unexpected losses have arisen or when incidents have occurred which indicate gaps in the control framework or in adherence to Group policies, the Risk Committee and the Audit Committee review special reports, prepared at the instigation of management, which analyse the cause of the issue, the lessons learned and the actions proposed by management to address the issue.

Employees

Health and safety

As part of the HSBC Group, HSBC UK is committed to providing a healthy and safe working environment for our employees, contractors, customers and visitors on HSBC Group premises, and where impacted by our operations. We aim to be compliant with all applicable health and safety legal requirements, and to ensure that best practice health and safety management standards are implemented and maintained across the Group.

Everyone in the HSBC Group has a responsibility for helping to create a healthy and safe working environment. Employees are expected to take ownership of their safety, and are encouraged and empowered to report any concerns.

Chief Operating Officers have overall responsibility for ensuring that the correct policies, procedures and safeguards are put into practice. This includes making sure that everyone in the HSBC Group has access to appropriate information, instruction, training and supervision.

Putting our commitment into practice, we delivered a range of programmes in 2019 to help us understand and manage effectively the risks we face and improve the buildings in which we operate:

We continued to deliver improvements in health and safety culture, through education and awareness programmes targeted at our areas of highest risk, which are construction and facilities management / maintenance activity.

We developed and implemented an improved health and safety training and awareness programme for all employees, ensuring roles and responsibilities were clear and understood. The programme, which included a new section for branch managers and staff, forms part of the mandatory annual training for all of our employees.

We implemented improved systems and processes for hazard identification and remediation. We also updated our suite of

management information dashboards to continually improve our awareness and management of our key risks.

An independent subject matter expert assessed our health and safety management system against the new international standard ISO 45001. The expert confirmed the robustness of our policies, procedures and processes, whilst identifying areas for continuous improvement.

Our safety management system was subjected to an extensive review by our independent internal audit team and resulted in zero high risk items being identified.

We continue to focus on enhancing the safety culture in our supply chain through our 'SAFER together' programme, building the awareness and capability to act and behave in the safest way.

We improved the Parenting Room facilities available to expectant mothers and new mothers returning to work in our large office buildings.

Employee health and safety

	Footnotes	2019	2018
Number of workplace fatalities		–	–
Number of RIDDOR reportable injuries	1	**15**	7
All injury rate per 100,000 employees		**1,559**	1,613

1 *RIDDOR – The Reporting of Injuries, Diseases and Dangerous Occurrences Regulations 2013.*

Well-being

At HSBC UK we recognise the value our people bring to the organisation. The well-being and engagement of our workforce is a key priority for us. We work with teams across every business area to develop initiatives and interventions that support our people and improve both their well-being confidence and capability.

We provide a range of tools, guidance and benefits to support our employees to enhance and improve their physical, mental and financial well-being.

We also provide a range of volunteering opportunities for employees to connect with local communities. We are investing in the knowledge and capability of our managers to help foster teams where people feel confident and comfortable in talking about well-being matters.

Diversity and inclusion

We are committed to enabling a thriving environment where our colleagues are valued, respected and supported to fulfil their potential; and where leveraging the range of ideas, backgrounds, styles and perspectives of our colleagues assists us in meeting the needs of our different stakeholder groups and driving better business outcomes for all. Our colleagues are expected to build positive and lasting relationships across the variety of people they interact with.

We focus on enhancing the diversity profile of our workforce so that it is more reflective of the communities we operate in and the customers we serve.

To support an inclusive environment, our policy is that each of us must treat colleagues with dignity and respect. We have zero tolerance for discrimination, bullying, harassment and victimisation on any ground, including age, race, ethnic or national origin, colour, mental or physical health conditions, disability, pregnancy, gender, gender expression, gender identity, sexual orientation, marital status or other domestic circumstances, employment status, working hours or other flexible working arrangements, or religion or belief. Such behaviour is considered a personal conduct matter and managed in accordance with applicable local policies and procedures and our consequence management framework.

Diversity and inclusion ('D&I') carries the highest level of executive support and as part of our commitment to shared ownership of the inclusion environment, we have implemented Driving Inclusion Workshops for our most senior and influential HSBC UK Leaders, as well as introducing an Inclusive Leadership objective to the performance scorecards of all HSBC UK People Managers.

More information about our diversity and inclusion activity is available under https://www.hsbc.com/our-approach.

Our focus on diversity and inclusion

We celebrate the diversity of our colleagues and customers and are taking actions to make sure that everyone is included in HSBC UK.

We have carried out a wide range of activities to celebrate and support diversity and inclusion. These include:

- Conducting a comprehensive review of every aspect of our hiring process to identify opportunities to improve our recruitment practices. As a result of our review, D&I training has been made available to our recruiters and we have implemented basic principles around how to approach conversations with hiring managers, challenging in the right way and alternative routes to market. These measures assist us in broadening our pool of diverse talent.
- We have completed the delivery of a programme of learning, development and coaching for our senior leaders so that they are enabled to drive inclusion in their areas of responsibility.
- Continuing to engage directly with our diverse colleges through our Employee Resource Groups and Communities. Our 16 groups have a total of 14,000 members. Our groups focus on gender, age, ethnicity, LGBT+, faith, working parents and carers, and ability. Our HSBC Communities cover a variety of topics including flexible working, mindfulness, military/ veterans, Chinese and Greek culture.

Supporting disabled colleagues

We believe in providing equal opportunities for all colleagues. The employment of colleagues with a disability is included in this commitment. The recruitment, training, career development and promotion of colleagues with a disability are based on the aptitudes and abilities of the individual. If a colleague becomes disabled whilst working for HSBC UK, our aim is to keep them working with us. Our dedicated Reasonable Adjustments Team will work with any colleague who becomes disabled and their manager to identify and implement reasonable adjustments aimed at keeping them in work.

Gender balance at senior leadership

We continue to focus on improving gender balance in senior leadership roles (classified as 0-3 in our global career band structure), with HSBC UK's intermediate goal on gender diversity being aligned to HSBC Group's global target of 30% of senior leadership roles held by women by 2020 (in line with our 30% Club CEO Campaign commitment). At HSBC UK, we have achieved 32% and we are continuing to focus on further improving our gender balance at a senior leadership level.

Employee development

The development of all our colleagues is essential to the future strength of our business and also in retaining high-calibre individuals with the values, skills and experience for current and future roles.

HSBC University, the home of learning at the HSBC Group, provides training programmes, educational resources and opportunities for connectivity, research and community engagement – with the core offering themed around leadership, risk management, strategy and performance, as well as business-specific technical training.

Over the last year, HSBC University has further developed its offering across all of the core strategic areas of focus mentioned. The effect of this is that at every level, there are programmes, materials and tools available that are designed to support every colleague on their own specific leadership development. Sustainability, Digital, and Wellbeing have been core for 2019 with HSBC UK front running dedicated learning for Mental Health Awareness training for all colleagues and a further enhanced face to face mental health training for all line managers.

Significant investment is being provided to help support the skills and development needs of the ever changing work-force and this will be the primary focus for 2020 as we gain momentum of understanding around the roles within banking of the future and how HSBC UK needs to support and grow each and every colleague to be successful.

Employee share schemes

The HSBC Group offers employees two options to voluntarily participate in Share purchase schemes helping to align the interests of employees with the creation of shareholder value. Our Sharesave plan allows employees to save an amount of money each month over a three- or five-year period and these savings can be used to purchase shares at a previously agreed discounted rate. Our Share Investment Plan allows employees to purchase shares each month from their pre-tax pay and should they be held for a minimum period of time, any proceeds from the sale of the shares are released free from tax or National Insurance contributions.

Auditor

PricewaterhouseCoopers LLP ('PwC') is external auditor to the bank. PwC has expressed its willingness to continue in office and the Board recommends that PwC be re-appointed as the bank's auditor. A resolution proposing the re-appointment of PwC as the bank's auditor and giving authority to the Audit Committee to determine its remuneration will be submitted to the forthcoming AGM.

Conflicts of interest and indemnification of Directors

The bank's Articles of Association give the Board authority to approve Directors' conflicts and potential conflicts of interest. The Board has adopted a policy and procedures for the approval of Directors' conflicts or potential conflicts of interest. The Board's powers to authorise conflicts are operating effectively and the procedures are being followed. A review of situational conflicts which have been authorised, including the terms of authorisation, is undertaken by the Board annually.

The Articles of Association provide that Directors and directors of associated companies are entitled to be indemnified out of the assets of the company against claims from third parties in respect of certain liabilities arising in connection with the performance of their functions, in accordance with the provisions of the UK Companies Act 2006. Such indemnity provisions have been in place during the financial year but have not been utilised by the Directors. All Directors have the benefit of directors' and officers' liability insurance.

Statement on going concern

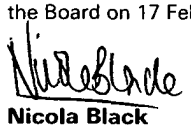
The Directors consider it appropriate to prepare the financial statements on a going concern basis. In making their going concern assessment, the Directors have considered a wide range of detailed information relating to present and potential conditions, including profitability, cash flows, capital requirements and capital resources.

Further information relevant to the assessment is provided in the Strategic Report and the Report of the Directors, in particular:

- A description of the group's strategic direction;
- A summary of the group's financial performance and a review of performance by business;
- The group's approach to capital management and its capital position; and
- The top and emerging risks facing the group, as appraised by the Directors, along with details of the group's approach to mitigating those risks and its approach to risk management in general.

In addition, the objectives, policies and processes for managing credit, liquidity and market risk are set out in the 'Report of the Directors: Risk'.

The Directors' Report comprising pages 17 to 60 was approved by the Board on 17 February 2020 and is signed on its behalf by:



Nicola Black

Company Secretary

HSBC UK Bank plc

Registered number 9928412

Disclosure of Information to the Auditor and Statement of Directors' Responsibilities

The Directors who held office at the date of approval of this Directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the bank's auditors are unaware; and each Director has taken all the steps that he ought to have taken as a Director to make himself aware of any relevant audit information and to establish that the company's auditors are aware of that information. The Directors are responsible for preparing the *Annual Report and Accounts 2019*, comprising the consolidated financial statements of the group and parent company financial statements for the bank in accordance with applicable laws and regulations.

Company law requires the Directors to prepare a Strategic Report, a Report of the Directors and group and parent company financial statements for each financial year. The Directors are required to prepare the group financial statements in accordance with IFRSs as adopted by the European Union and have elected to prepare the bank's financial statements on the same basis.

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the group and bank and of their profit or loss for that period. In preparing each of these financial statements, the Directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether they have been prepared in accordance with IFRSs as adopted by the European Union; and
- prepare the financial statements on a going concern basis unless it is not appropriate. Since the Directors are satisfied that the group has the resources to continue in business for the foreseeable future, the financial statements continue to be prepared on a going concern basis.

The Directors have responsibility for ensuring that sufficient accounting records are kept that disclose with reasonable accuracy at any time the financial position of the bank and enable them to ensure that its financial statements comply with the Companies Act 2006. They are responsible for safeguarding the assets of the Company and the group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The Directors have responsibility for the maintenance and integrity of the Annual Report and Accounts 2019 as they appear on the bank's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Each of the Directors, the names of whom are set out in the Governance section of the Directors' Report on pages 54 and 55 of the Annual Report and Accounts 2019, confirm to the best of their knowledge:

- In accordance with rule 4.1.12(3)(a) of the Disclosure Rules and Transparency Rules, the consolidated financial statements, which have been prepared in accordance with IFRSs as issued by the IASB and as endorsed by the European Union, have been prepared in accordance with the applicable set of accounting standards and give a true and fair view of the assets, liabilities, financial position and profit or loss of the bank and the undertakings included in the consolidation taken as a whole; and
- The management report represented by the Strategic Report and Directors' Report has been prepared in accordance with rule 4.1.12(3)(b) of the Disclosure Rules and Transparency Rules, and includes a fair review of the development and performance of the business and the position of the bank and the undertakings included in the consolidation as a whole, together with a description of the principal risks and uncertainties that the group faces.

Approved by the Board on 17 February 2020 and signed on its behalf by:

Nicola Black

Company Secretary

HSBC UK Bank plc

Registered number 9928412

Independent auditors' report to the member of HSBC UK Bank plc

Report on the audit of the financial statements

Opinion

In our opinion, HSBC UK Bank plc's group financial statements and parent company financial statements (the 'financial statements'):

- give a true and fair view of the state of the group's and of the parent company's affairs as at 31 December 2019 and of the group's profit and the group's and the parent company's cash flows for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards ('IFRSs') as adopted by the European Union and, as regards the parent company's financial statements, as applied in accordance with the provisions of the Companies Act 2006; and
- have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation.

We have audited the financial statements, included within the Annual Report and Accounts (the 'Annual Report'), which comprise:

- the consolidated income statement for the year ended 31 December 2019;
- the consolidated statement of comprehensive income for the year ended 31 December 2019;
- the consolidated balance sheet at 31 December 2019;
- the consolidated statement of cash flows for the year ended 31 December 2019;
- the consolidated statement of changes in equity for the year ended 31 December 2019;
- the HSBC UK Bank plc balance sheet at 31 December 2019;
- the HSBC UK Bank plc statement of cash flows for the year ended 31 December 2019;
- the HSBC UK Bank plc statement of changes in equity for the year ended 31 December 2019; and
- the notes to the financial statements, which include a description of the significant accounting policies.

Our opinion is consistent with our reporting to the Audit Committee.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities under ISAs (UK) are further described in the Auditors' responsibilities for the audit of the financial statements section of our report. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

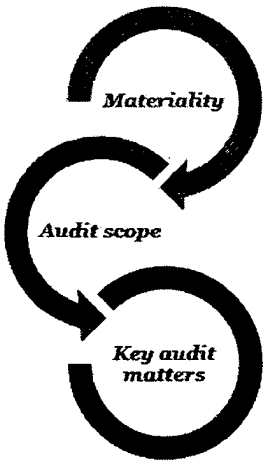
We remained independent of the group in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, which includes the Financial Reporting Council's ('FRC') Ethical Standard, as applicable to listed public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

To the best of our knowledge and belief, we declare that non-audit services prohibited by the FRC's Ethical Standard were not provided to the group or the parent company.

Other than those disclosed in note 4 to the financial statements, we have provided no non-audit services to the group or the parent company in the period from 1 January 2019 to 31 December 2019.

Our audit approach

Overview



- Overall group materiality: £107m (2018: £65m), based on 5% of adjusted profit before tax.
- Overall parent company materiality: £93m (2018: £57m), based on 5% of adjusted profit before tax.

- HSBC UK Bank plc is a member of the HSBC Group, the ultimate parent company of which is HSBC Holdings plc. HSBC UK Bank plc operates in the UK.
- We performed an audit of the complete financial information of three reporting units, namely HSBC UK Bank plc, Marks and Spencer Financial Services plc ('M&S') and HSBC Private Bank (UK) Limited ('Private Bank').
- For two further reporting units, specific audit procedures were performed over selected significant account balances.

The following areas were identified as key audit matters for the group and parent company. These are discussed in further detail in the Appendix:

- Customer Redress - Payment Protection Insurance ('PPI')
- Provision for conduct related matters other than PPI
- Expected credit loss ('ECL') provision for loans and advances
- Valuation of goodwill relating to the Private Banking ('PB') cash generating unit ('CGU')
- Recognition of income under Effective Interest Rate accounting
- Valuation of defined benefit pension obligation
- Information Technology ('IT') Access Management

The scope of our audit

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the financial statements. In particular, we looked at where the directors made subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain.

Capability of the audit in detecting irregularities, including fraud

Based on our understanding of the group and industry, we identified that the principal risks of non-compliance with laws and regulations include, but are not limited to, the Financial Conduct Authority's regulations, the Prudential Regulation Authority's regulations, UK Listing Rules, Pensions legislation and the UK tax legislation. We considered the extent to which non-compliance might have a material effect on the financial statements. We also considered those laws and regulations that have a direct impact on the preparation of the financial statements such as the Companies Act 2006. We evaluated management's incentives and opportunities for fraudulent manipulation of the financial statements (including the risk of override of controls), and determined that the principal risks were related to posting inappropriate journal entries to increase revenue or reduce expenditure, and management bias in accounting estimates. Our audit procedures included challenging estimates and judgements made by management in their significant accounting estimates, in particular in relation to the expected credit loss provisions of loans and advances to customers, valuation of goodwill relating to the PB CGU, and provisioning for PPI and other conduct related matters (see related key audit matters in the Appendix), and identifying and testing journal entries, in particular journal entries posted with unusual account combinations or posted by senior management. The group engagement team shared this risk assessment with the component auditors so that they could include appropriate audit procedures in response to such risks in their work. Audit procedures performed by the group engagement team and/or component auditors included review of the financial statement disclosures to underlying supporting documentation, review of correspondence with and reports to the regulators, review of correspondence with legal advisors, enquiries of management, enquiries of legal counsel and review of internal audit reports in so far as they related to the financial statements.

There are inherent limitations in the audit procedures described above and the further removed non-compliance with laws and regulations is from the events and transactions reflected in the financial statements, the less likely we would become aware of it. Also, the risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion.

Key audit matters

Key audit matters are those matters that, in the auditors' professional judgement, were of most significance in the audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by the auditors, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. These matters, and any comments we make on the results of our procedures thereon, were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. This is not a complete list of all risks identified by our audit. The key audit matters are discussed further in the Appendix.

How we tailored the audit scope

We tailored the scope of our audit to ensure that we performed enough work to be able to give an opinion on the financial statements as a whole, taking into account the structure of the group and the parent company, the accounting processes and controls, and the industry in which they operate.

HSBC UK Bank plc is structured into four divisions being Retail Banking and Wealth Management, Commercial Banking, Private Banking and Global Banking and Markets. The divisions operate across a number of operations and subsidiary entities in the United Kingdom. Within the group's main consolidation and financial reporting system, the consolidated financial statements are an aggregation of the operations and subsidiary entities ('reporting units'). Each reporting unit submits their financial information to the group in the form of a consolidation pack. .

In establishing the overall approach to the group and parent company audit, we scoped our work using the balances included in the consolidation pack. We determined the type of work that needed to be performed over the reporting units by us, as the group engagement team, or auditors within PwC UK operating under our instruction ('component auditors').

As a result of our scoping, for the parent company we determined that an audit of the complete financial information of HSBC UK Bank plc was necessary, owing to its financial significance. For group purposes, we additionally performed an audit of the complete financial information of M&S and Private Bank. We instructed component auditors, PwC UK, to perform the audits of these reporting units. Our interactions with component auditors included regular communication throughout the audit, the issuance of instructions, a review of working papers relating to the key audit matters and formal clearance meetings. The group audit engagement partner was also the partner on the audit of the HSBC UK Bank plc and Private Bank significant reporting units.

We then considered the significance of other reporting units in relation to primary statement account balances. In doing this we also considered the presence of any significant audit risks and other qualitative factors (including history of misstatements through fraud or error). For two reporting units, specific audit procedures were performed over selected significant account balances. For the remainder, the risk of material misstatement was mitigated through group audit procedures including testing of entity level controls and subsidiary level analytical review procedures.

Certain group-level account balances (including goodwill) were audited by the group engagement team.

Materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures on the individual financial statement line items and disclosures and in evaluating the effect of misstatements, both individually and in aggregate on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

	Group financial statements	Parent company financial statements
Overall materiality	£107m (2018: £65m)	£93m (2018: £57m)
How we determined it	5% of adjusted profit before tax	5% of adjusted profit before tax
Rationale for benchmark applied	Adjusted profit before tax is the primary measure used by shareholders in assessing the performance of the group and the parent company and removes the impact of significant items that distort year-on-year comparisons. In determining overall materiality, we have excluded costs relating to customer redress programmes as they are large, one-off items unrelated to the underlying performance of the group and parent company.	

For each component in the scope of our group audit, we allocated a materiality that is less than our overall group materiality. The range of materiality allocated across reporting units was between £10.8m and £93m. Certain reporting units were audited to a local statutory audit materiality that was also less than our overall group materiality.

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £4.6m (Group audit) (2018: £2.8m) and £4.6m (Parent company audit) (2018: £2.8m) as well as misstatements below those amounts that, in our view, warranted reporting for qualitative reasons.

Conclusions relating to going concern

ISAs (UK) require us to report to you when:

- the directors' use of the going concern basis of accounting in the preparation of the financial statements is not appropriate; or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the group's and parent company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

We have nothing to report in respect of the above matters.

However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the group's and parent company's ability to continue as a going concern. For example, the terms of the United Kingdom's withdrawal from the European Union are not clear, and it is difficult to evaluate all of the potential implications on the group and parent company's trade, customers, suppliers and the wider economy.

Reporting on other information

The other information comprises all of the information in the Annual Report other than the financial statements and our auditors' report thereon. The directors are responsible for the other information. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except to the extent otherwise explicitly stated in this report, any form of assurance thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we identify an apparent material inconsistency or material misstatement, we are required to perform procedures to conclude whether there is a material misstatement of the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report based on these responsibilities.

With respect to the Strategic Report and Report of the Directors, we also considered whether the disclosures required by the UK Companies Act 2006 have been included.

Based on the responsibilities described above and our work undertaken in the course of the audit, ISAs (UK) require us also to report certain opinions and matters as described below.

Strategic Report and Report of the Directors

In our opinion, based on the work undertaken in the course of the audit, the information given in the Strategic Report and Report of the Directors for the year ended 31 December 2019 is consistent with the financial statements and has been prepared in accordance with applicable legal requirements.

In light of the knowledge and understanding of the group and parent company and their environment obtained in the course of the audit, we did not identify any material misstatements in the Strategic Report and Report of the Directors.

Responsibilities for the financial statements and the audit

Responsibilities of the directors for the financial statements

As explained more fully in the Statement of Directors' Responsibilities in respect of the financial statements set out on page 60, the directors are responsible for the preparation of the financial statements in accordance with the applicable framework and for being satisfied that they give a true and fair view. The directors are also responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the group's and the parent company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the group or the parent company or to cease operations, or have no realistic alternative but to do so.

Auditors' responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: www.frc.org.uk/ auditors responsibilities. This description forms part of our auditors' report.

Use of this report

This report, including the opinions, has been prepared for and only for the parent company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

Other required reporting

Companies Act 2006 exception reporting

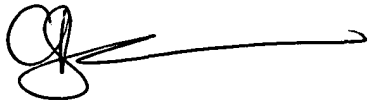
Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the parent company, or returns adequate for our audit have not been received from branches not visited by us; or
- certain disclosures of directors' remuneration specified by law are not made; or
- the parent company financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

Appointment

Following the recommendation of the audit committee, we were appointed by the members on 7 August 2017 to audit the financial statements for the year ended 31 December 2017 and subsequent financial periods. The period of total uninterrupted engagement is 3 years, covering the years ended 31 December 2017 to 31 December 2019.



Carl Sizer *(Senior Statutory Auditor)*

for and on behalf of PricewaterhouseCoopers LLP

Chartered Accountants and Statutory Auditors

Birmingham

17 February 2020

Appendix: Key audit matters discussed with the Audit Committee

The key audit matters are discussed below together with an explanation of how the audit was tailored to address these specific areas.

All key audit matters are applicable to both the group and parent company.

Customer Redress - Payment Protection Insurance ('PPI')

Nature of key audit matter	Matters discussed with the Audit Committee
The provision for customer redress in respect of PPI incorporates a number of estimates that are highly judgemental. A high volume of information requests and complaints were received in the run up to the timebar on the 29 August 2019. As a result of the volumes received a significant number are yet to be assessed for mis-selling. The validity rate applied to the information requests and the average redress for these cases including those in respect of the complaints brought by the Official Receiver are the key estimates underlying the provision. An estimate has also been made in relation to potential future legal claims where volumes are difficult to predict.	We discussed with the Audit Committee the appropriateness of applying historic validity rates and average redress to the remaining information requests. We discussed the adequacy of provisions for matters not impacted by timebar, including Official Receiver complaints and legal claims. We discussed the results of our controls and substantive testing. We also discussed alternative scenarios and the range of sensitivity in concluding on the adequacy of the provision held. No material misstatements have been identified from our work.

Procedures performed to support our discussions and conclusions

- Evaluated the design and tested the operating effectiveness of key controls over the process of capturing key data used in the PPI provision calculation model.
- Examined the modelling process around the PPI provision calculation. Tested historical validity rates, and redress amounts with worked cases and assessed whether the estimates underpinning the provision calculations, including future trends expected in respect of these inputs, were appropriate.
- Tested historic data relating to the number of legal claims received and assessed whether the assumptions relating to future volumes were appropriate.
- Considered the sensitivity of the provision to possible variations in estimates. This could result in different amounts for some provisions to those calculated however these differences were within a reasonable range of outcomes.
- Observed management's review and challenge forums to assess the appropriateness of the provision.
- Evaluated whether the disclosures within the financial statements appropriately address the significant uncertainties that exist around determining the provisions and the sensitivity of the provisions to changes in the underlying estimates by comparing to the output of our audit work.

Relevant references in the Annual Report and Accounts 2019

Note 1: Basis of preparation and significant accounting policies 1.2(j) Provisions, page 85.
Note 19: Provisions, page 103.

Provision for conduct related matters other than PPI

Nature of key audit matter	Matters discussed with the Audit Committee
A number of deficiencies have been identified in the Bank's internal processes that have resulted in customer detriment. The provision for these matters reflects the expected cost of repayment of historic fees and interest, distress and inconvenience payments and related operational remediation activities. Management grouped customers into cohorts based on the nature of the matter. The volume of customers impacted and expected redress amounts to be paid are the key estimates underlying the provision. Few customer redress payments have been made to date and the population of impacted customers is still being identified. The data available to support these estimates is limited, making them highly subjective.	We discussed with the Audit Committee the process performed by management to estimate the impacted populations. We also discussed the estimates used in determining the expected redress for each cohort. We discussed the results of our controls and substantive testing. We also discussed alternative scenarios and the range of sensitivity in concluding on the adequacy of the provision held. No material misstatements have been identified from our work.

Procedures performed to support our discussions and conclusions

- Evaluated the design and tested the operating effectiveness of key controls over key inputs to the calculated provision.
- Evaluated the completeness of impacted cohorts identified by management by comparing these to customer populations expected to be affected by process deficiencies.
- Examined the appropriateness of the provisioning model and underlying estimates used. Tested the appropriateness of customer populations identified for each cohort and the estimated redress per customer.
- Considered the sensitivity of the provision to possible changes in outcome. Considered the different amounts calculated to be within a reasonable range of outcomes.
- Observed management's review and challenge forums to assess the appropriateness of the provision.
- Evaluated whether the disclosures within the financial statements appropriately address the uncertainties inherent to determining the provision and the sensitivity of the provision to changes in key estimates by comparing to the output of our audit work.

Relevant references in the Annual Report and Accounts 2019

Note 1: Basis of preparation and significant accounting policies 1.2(j) Provisions, page 85.
Note 19: Provisions, page 103.

Expected credit loss ('ECL') provision for loans and advances

Nature of key audit matter	Matters discussed with the Audit Committee
The ECL provision for loans and advances has a significant number of data inputs for both the retail and wholesale portfolios. In addition to the data inputs a number of key judgements are used to estimate the ECL provision, in particular the severity and likelihood of alternative downside economic scenarios that form part of the forward economic guidance, the determination of customer credit ratings and probabilities of default and loss rates that go into the expected credit loss models and the estimation of specific impairments for wholesale exposures. Whilst the credit environment has remained largely benign as a result of low interest rates and low unemployment, broader economic risks such as the impact of the UK departure from the EU remain which increase the estimation uncertainty in the ECL.	We discussed with the Audit Committee changes to risk factors and other inputs within the models, geopolitical risks, such as the terms of the UK's departure from the EU; the migration of customer risk ratings; and impairments of significant wholesale exposures. We discussed the more judgemental decisions made by management, in particular the severity and likelihood of alternative downside economic scenarios that form part of the forward economic guidance including their impact on ECL and consideration of required post model adjustments, including the impact of model and data limitations. We also discussed how the control environment over the calculation of ECL evolved following initial adoption, reporting on areas of improvement and the results of our testing. No material misstatements have been identified from our work.

Procedures performed to support our discussions and conclusions

- Utilised our credit modelling specialists to perform risk risk based substantive testing of models that were updated during the year, including independently rebuilding the modelling for certain estimates.
- Independently reviewed the updates to the scripts used in the underlying tool to calculate ECL to validate that they reflected approved updates to models, parameters and inputs.
- Controls over the inputs of critical data into source system and the flow and transformation of data between source systems to the impairment calculation engine were tested. Substantive testing was performed over the critical data used in the year end ECL calculation.
- Tested the review and challenge of multiple economic scenarios by an expert panel and internal governance committee, and assessed the reasonableness and likelihood of these scenarios using our economic experts. Relevant economic, political and other events were considered in assessing the reasonableness of alternative downside scenarios. The severity and magnitude of the scenarios were compared to external forecasts and data from historical economic downturns, and the sensitivities of the scenarios on the ECL were considered.
- Observed management's review and challenge forums to assess the ECL output and approval of post model adjustments.
- Tested the approval of the key inputs, estimates and discounted cash-flows that support the impairments of significant wholesale exposures, and substantively tested a sample of significant wholesale exposures.

Relevant references in the Annual Report and Accounts 2019

Note 1: Basis of preparation and significant accounting policies 1.2(g) Impairment of amortised cost and FVOCI financial assets, page 82.
Summary of credit risk, page 26
Measurement uncertainty and sensitivity analysis of ECL estimates, page 31.

Valuation of goodwill relating to the Private Banking ('PB') cash generating unit ('CGU')

Nature of key audit matter	Matters discussed with the Audit Committee
The macroeconomic and geopolitical environment in which the group operates has become more challenging, impacting both 2019 earnings and the outlook into 2020. Furthermore, a strategy update has been announced by HSBC Holdings plc that may impact the future profitability of certain businesses across the group. These matters were considered a potential indicator of impairment of the goodwill held by the group in respect of Private Banking ('PB') cash generating unit ('CGU'). An impairment test was performed by the Bank using a value in use ('VIU') model that estimates the value of the PB CGU. The VIU is £218m in excess of the carrying value for this CGU. This is highly sensitive to estimates within the model. The determination of the VIUs is based on the requirements of the accounting standard IAS 36 'Impairment of assets' and estimates about future cash flows which are estimated using the group's Annual Operating Plan ('AOP'), long term growth rates and discount rates. These estimates, which are judgemental, are derived from a combination of management estimates, market data and other information provided by external parties.	We discussed the appropriateness of the VIU estimates with the Audit Committee, particularly those for which variations had the most significant impact on the VIU estimate. We focused on the estimates related to the growth rate targets in the AOP, and the long term growth rates and discount rates for PB. Our discussions and focus on estimates was driven by consideration of the achievability of management's AOP and the prospects for the private banking business in the future. No material misstatements have been identified from our work.

Procedures performed to support our discussions and conclusions

- Assessed the appropriateness of the methodology, including the estimation of VIU.
- Reasonable ranges for the discount rates and terminal growth rates used within the model were independently calculated with the assistance of our valuation experts, and compared to the rates used by management.
- Recalculated terminal growth rates used within the model utilising external market data, and compared to the rates used by management.
- Inputs used in the determination of estimations within the model including the Annual Operating Plan were challenged.
- Assessed whether the cash flows included in the model were in accordance with the relevant accounting standard.
- Performed sensitivity analysis on key estimates used, both individually and in aggregate.
- The controls in place over the model, and its mathematical accuracy, were tested.
- Evaluated whether the disclosures within the Annual Report and Accounts 2019 appropriately address the significant estimates used to determine the impairment of goodwill.

Relevant references in the Annual Report and Accounts 2019

Note 1: Basis of preparation and significant accounting policies 1.2(a) Consolidation and related policies, page 79.
Note 15: Goodwill and intangible assets, page 100.

Recognition of income under Effective Interest Rate accounting

Nature of key audit matter	Matters discussed with the Audit Committee
Loans and advances are recognised at amortised cost, and interest income recognised using the Effective Interest Rate (EIR) method. The majority of interest income is calculated by automated systems and requires little or no management judgement. Therefore we focused our work in relation to revenue recognition on EIR accounting and specifically credit cards. EIR accounting is inherently subjective as it requires management to predict customer behaviour into the future, over the expected life of the products, on which the EIR adjustment calculation is based. Changes in the key estimates could have a material impact on the EIR adjustments and hence the revenue recognised in any one accounting period. For credit cards there are significant judgments in calculating the EIR adjustment including setting estimates relating to the retention of customer balances over the expected life, the proportion that remain active following the end of the promotional period and the related interest income earned on those balances. Management have estimated the impact that persistent debt regulations will have on customer behaviour and therefore on the accrued interest balance. This included assessing the proportion of customers who will take up each of the options offered by the bank, including increasing credit card repayments or switching to alternative products and considering those who may have cards suspended.	Discussions with the Audit Committee focused on the key judgments and estimates including the level of expected customer balances and interest yield on significant promotional offers, the retention of balances after the end of the promotional period and consideration as to how the Group's historic experience is consistent with that expected in the future. We discussed the impact on key estimates of judgements applied in response to the FCA's proposed changes to rules impacting customers in persistent debt. We also discussed the results of our audit work including testing of management controls, substantive testing and evaluation of the application of accounting standards. No material misstatements have been identified from our work.

Procedures performed to support our discussions and conclusions

- Tested the controls over data input and checked the accuracy of model calculations.
- Observed management's governance meetings for the setting, challenge and approval of key estimates, including monitoring of actual trends compared to forecast estimates.
- Tested the governance over product pricing models and the use of that output to support the determination of EIR at origination.
- Tested the appropriateness of models used by management in EIR calculations and critically assessed and challenged the appropriateness of the key estimates, including expected life of customer accounts and assessing whether the use of customer balance and yield curves based on historic data were appropriately reflective of current behaviour and an appropriate indicator of the future.
- Performed sensitivity analyses of key estimates to understand the materiality of the impact that potential realistic changes in estimates may have, either individually or in combination, on the EIR asset.
- Performed testing over the adjustments taken to revenue during the year as a result of persistent debt regulations, considering the appropriateness of estimates made around the contact programme, customer responsiveness and resulting actions, and the completeness of the populations identified.
- Assessed the sufficiency of the disclosures in the financial statements relating to significant estimates made in the EIR calculation, including disclosure of sensitivities.

Relevant references in the Annual Report and Accounts 2019

Note 1: Basis of preparation and significant accounting policies 1.2(b) Income and expense, page 80.

Valuation of defined benefit pension obligation

Nature of key audit matter	Matters discussed with the Audit Committee
The valuation of the defined benefit obligations of the HSBC Bank (UK) Pension Scheme is dependent on a number of actuarial estimates, including the discount rate, inflation rate and mortality rates. Management uses actuarial experts to determine the valuation of the defined benefit obligation using a number of market based inputs and other financial and demographic estimates. The estimates were updated to reflect market decreases in the discount rate and to reflect changing market practice and management's views of long term inflation. Mortality rates were updated to reflect the latest data for life expectancy. Changes in these estimates can have a material impact on the valuation due to the long duration of the pension obligations and as such the valuation is considered highly judgemental.	We discussed with the Audit Committee the key judgments made by management in setting the actuarial estimates used to determine the value of the defined benefit obligations. We also discussed the results of the work performed by our actuarial experts and how the estimates compare to our independently compiled expected range. No material misstatements have been identified from our work.

Procedures performed to support our discussions and conclusions

- Tested the controls for determining the actuarial estimates used in calculating the valuation of future pension obligations and the approval of those estimates by senior management.
- Engaged our actuarial experts to understand the judgements made by management and managements' actuarial expert in determining the key financial and demographic estimates used in the calculation of the liability.
- Assessed the reasonableness of the estimates using independently developed benchmarks and external market data.
- Evaluated management's approach to derive the discount rate and inflation estimates and compared this to market practice.
- Evaluated the appropriateness of the disclosures within the financial statements, including the disclosure regarding the sensitivity of estimates by comparing them to the output of our audit work.

Relevant references in the Annual Report and Accounts 2019

Note 1: Basis of preparation and significant accounting policies 1.2(h) Employee compensation and benefits, page 85.
Note 3: Employee compensation and benefits, page 86.

Information Technology ('IT') Access Management

Nature of key audit matter	Matters discussed with the Audit Committee
Our audit approach relies extensively on automated controls and therefore on the effectiveness of controls over IT systems. In previous years, we identified and reported that controls over access to applications, operating systems and data in the financial reporting process required improvements. Access management controls are critical to ensure that changes to applications and underlying data are made in an appropriate manner. Appropriate access and change controls contribute to mitigating the risk of potential fraud or errors as a result of changes to applications and data. Management implemented remediation activities that have contributed to progress being made in reducing the risk over access management in the financial reporting process. Controls continue to require some improvement going forward.	The significance of IT controls to our audit and the status of the remediation was discussed at the Audit Committee meetings during the year. No material misstatements have been identified from our work.

Procedures performed to support our discussions and conclusions

Access rights were tested over applications, operating systems and databases relied upon for financial reporting. Specifically, the audit tested that:

- new access requests for joiners were properly reviewed and authorised;
- user access rights were removed on a timely basis when an individual left or moved role;
- access rights to applications, operating systems and databases were periodically monitored for appropriateness; and
- highly privileged access was restricted to appropriate personnel.

Other areas that were independently assessed included: password policies; security configurations; controls over changes to code, data and config; and that the ability to make such change via privileged operating system or databases access in the production environment was appropriately restricted.

Where control deficiencies were identified, a range of other procedures were performed:

- where access outside of policy was identified, we understood the nature of the access, and, where required, obtained additional evidence on whether that access had been exploited;
- testing of remediated controls to manage the monitoring of business access, including access that would allow a user to potentially override segregations of duty; and
- substantive testing of whether users inappropriately hold access to key functionality underpinning financial reporting processes, specific year-end reconciliations (i.e. custodian, bank account and suspense account reconciliations) and confirmations with external counterparties.

Financial statements

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Consolidated income statement
for the year ended 31 December

	Notes	2019[5] £m	2018 £m
Net interest income		**4,752**	2,456
– interest income[1,2,3]		**5,696**	2,805
– interest expense[4]		**(944)**	(349)
Net fee income	2	**1,230**	648
– fee income		**1,456**	831
– fee expense		**(226)**	(183)
Net income from financial instruments held for trading or managed on a fair value basis		**400**	198
Changes in fair value of other financial instruments mandatorily measured at fair value through profit or loss		**2**	—
Gains less losses from financial investments		**48**	22
Other operating income		**52**	33
Total operating income		**6,484**	3,357
Net operating income before change in expected credit losses and other credit impairment charges		**6,484**	3,357
Change in expected credit losses and other credit impairment charges		**(613)**	(305)
Net operating income		**5,871**	3,052
Employee compensation and benefits	3	**(934)**	(611)
General and administrative expenses		**(3,601)**	(1,267)
Depreciation and impairment of property, plant and equipment and right-of-use assets		**(170)**	(46)
Amortisation and impairment of intangible assets		**(156)**	(64)
Total operating expenses		**(4,861)**	(1,988)
Operating profit		**1,010**	1,064
Profit before tax		**1,010**	1,064
Tax expense	5	**(494)**	(301)
Profit for the year		**516**	763
Attributable to:			
– ordinary shareholders of the parent company		**512**	763
– non-controlling interests		**4**	—

1 *Interest income recognised on financial assets measured at amortised cost is £5,459m (2018: £2,722m).*
2 *Interest income recognised on financial assets measured at FVOCI is £237m (2018: £81m).*
3 *Interest revenue calculated using the effective interest method comprises interest recognised on financial assets measured at either amortised cost or fair value through other comprehensive income.*
4 *Interest expense on financial instruments, excluding interest on trading liabilities designated or otherwise mandatorily measured at fair value is £943m (2018: £349m).*
5 *HSBC UK's banking operations commenced on 1 July 2018. To provide better comparative information, the summary income statement is presented for the six months to 30 June 2019 and 31 December 2019 on Page 10 in the Strategic Report.*

Consolidated statement of comprehensive income

for the year ended 31 December

	2019 £m	2018 £m
Profit for the year	**516**	763
Other comprehensive income		
Items that will be reclassified subsequently to profit or loss when specific conditions are met:		
Debt instruments at fair value through other comprehensive income	**(4)**	10
– fair value gains	**42**	34
– fair value gains transferred to the income statement on disposal	**(48)**	(21)
– expected credit losses recognised in the income statement	**1**	–
– income taxes	**1**	(3)
Cash flow hedges	**34**	(17)
– fair value gains/(losses)	**39**	(107)
– fair value losses reclassified to the income statement	**7**	84
– income taxes	**(12)**	6
Exchange differences	**1**	(2)
– other exchange differences	**1**	(2)
Items that will not be reclassified subsequently to profit or loss:		
Remeasurement of defined benefit asset/liability	**(207)**	(364)
– before income taxes	**(268)**	(485)
– income taxes	**61**	121
Other comprehensive expense for the year, net of tax	**(176)**	(373)
Total comprehensive income for the year	**340**	390
Attributable to:		
– ordinary shareholders of the parent company	**336**	390
– non-controlling interests	**4**	–
Total comprehensive income for the year	**340**	390

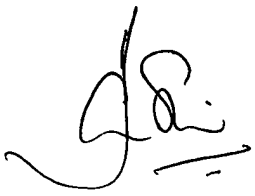
Consolidated balance sheet

at 31 December

	Notes	2019 £m	2018 £m
Assets			
Cash and balances at central banks		**37,030**	33,193
Items in the course of collection from other banks		**504**	603
Financial assets designated and otherwise mandatorily measured at fair value through profit or loss	7	**66**	35
Derivatives	9	**121**	66
Loans and advances to banks		**1,389**	1,263
Loans and advances to customers		**183,056**	174,807
Reverse repurchase agreements – non-trading		**3,014**	3,422
Financial investments	10	**19,737**	13,203
Prepayments, accrued income and other assets	16	**8,203**	8,528
Interests in joint ventures	12	**9**	9
Goodwill and intangible assets	15	**3,973**	3,810
Total assets		**257,102**	238,939
Liabilities and equity			
Liabilities			
Deposits by banks		**529**	1,027
Customer accounts		**216,214**	204,837
Repurchase agreements – non-trading		**98**	639
Items in the course of transmission to other banks		**343**	233
Derivatives	9	**201**	346
Debt securities in issue	17	**3,142**	–
Accruals, deferred income and other liabilities	18	**1,834**	2,409
Current tax liabilities		**409**	359
Provisions	19	**1,325**	630
Deferred tax liabilities	5	**1,223**	1,189
Subordinated liabilities	20	**9,533**	4,937
Total liabilities		**234,851**	216,606
Equity			
Called up share capital	23	**–**	–
Share premium account	23	**9,015**	9,015
Other equity instruments	23	**2,196**	2,196
Other reserves		**7,688**	7,657
Retained earnings		**3,292**	3,405
Total shareholders' equity		**22,191**	22,273
Non-controlling interests		**60**	60
Total equity		**22,251**	22,333
Total liabilities and equity		**257,102**	238,939

The accompanying notes on pages 78 to 118, and the audited sections in: the 'Financial Summary' on pages 10 to 15 and the 'Report of the Directors' on pages 17 to 60 form an integral part of these financial statements.

These financial statements were approved by the Board of Directors on 17 February 2020 and signed on its behalf by:



John David Stuart

Director

Consolidated statement of cash flows

for the year ended 31 December

	2019 £m	2018 £m
Profit before tax	**1,010**	1,064
Adjustments for non-cash items:		
Depreciation and amortisation[1]	**326**	110
Net gain from investing activities	**(49)**	–
Change in expected credit losses gross of recoveries and other credit impairment charges	**697**	364
Provisions including pensions	**1,248**	184
Share-based payment expense	**17**	–
Elimination of exchange differences[2]	**255**	(190)
Changes in operating assets and liabilities		
Change in net trading securities and derivatives	**(161)**	(33)
Change in loans and advances to banks and customers	**(8,306)**	(7,346)
Change in reverse repurchase agreements – non-trading	**408**	(3,422)
Change in financial assets designated and otherwise mandatorily measured at fair value	**(31)**	(27)
Change in other assets	**511**	1,941
Change in deposits by banks and customer accounts	**10,879**	4,102
Change in repurchase agreements – non-trading	**(541)**	639
Change in debt securities in issue	**3,142**	–
Change in other liabilities	**(1,621)**	(4,576)
Contributions paid to defined benefit plans	**(115)**	(80)
Tax paid	**(360)**	(74)
Net cash from operating activities	**7,309**	(7,344)
Purchase of financial investments	**(19,300)**	(5,369)
Proceeds from the sale and maturity of financial investments	**12,629**	3,292
Net cash flows from the purchase and sale of property, plant and equipment	**(69)**	(57)
Net investment in intangible assets	**(319)**	(164)
Net cash flow on acquisition of subsidiaries, businesses and joint venture[3]	**—**	29,410
Net cash from investing activities	**(7,059)**	27,112
Issue of ordinary share capital and other equity instruments	**—**	9,000
Subordinated loan capital issued[4]	**4,619**	2,020
Funds received from the shareholder of the parent company	**—**	3,000
Dividends paid to shareholders of the parent company and non-controlling interests	**(455)**	(1)
Net cash from financing activities	**4,164**	14,019
Net increase in cash and cash equivalents	**4,414**	33,787
Cash and cash equivalents at 1 Jan	**33,817**	2
Exchange differences in respect of cash and cash equivalents	**(145)**	28
Cash and cash equivalents at 31 Dec[5]	**38,086**	33,817
Cash and cash equivalents comprise:		
– cash and balances at central banks	**37,030**	33,193
– items in the course of collection from other banks	**504**	603
– loans and advances to banks of one month or less	**787**	105
– treasury bills, other bills and certificates of deposit less than three months	**23**	149
– cash collateral and net settlement accounts	**85**	–
– less: items in the course of transmission to other banks	**(343)**	(233)
Cash and cash equivalents at 31 Dec[5]	**38,086**	33,817

Interest received was £5,648m (2018: £2,574m), interest paid was £987m (2018: £228m).

1 *The impact of the right-of-use assets recognised under IFRS 16 at the beginning of 2019 is not recognised in 2018.*
2 *Adjustment to bring changes between opening and closing balance sheet amounts to average rates. This is not done on a line-by-line basis, as details cannot be determined without unreasonable expense.*
3 *No cash or cash equivalent was paid in consideration of the investment in subsidiaries and joint venture as it formed part of the Part VII transfer of asset and liabilities. The aggregate amount of cash and cash equivalent in the subsidiaries and other businesses over which control was obtained was £29,410m.*
4 *Subordinated liabilities changes during the year are attributable to cash flows from issuance of securities of £4,619m (2018: £2,020m). Non-cash changes during the year included foreign exchange (loss) of £(23)m (2018: Nil).*
5 *At 31 December 2019 £627m (2018: £363m) was not available for use by the group, all related to mandatory deposits at central banks (2018: £363m).*

Consolidated statement of changes in equity

for the year ended 31 December

	Called up share capital and share premium	Other equity instruments	Retained earnings	Other reserves: Financial assets at FVOCI reserve	Cash flow hedging reserve	Foreign exchange reserve	Group re-organisation reserve	Total shareholders' equity	Non-controlling interests	Total equity
	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
At 1 Jan 2019	**9,015**	**2,196**	**3,405**	**14**	**(46)**	**(2)**	**7,691**	**22,273**	**60**	**22,333**
Profit for the year	–	–	512	–	–	–	–	512	4	510
Other comprehensive income (net of tax)	–	–	(207)	(5)	34	2	–	(176)	–	(176)
– debt instruments at fair value through other comprehensive income	–	–	–	(4)	–	–	–	(4)	–	(4)
– cash flow hedges	–	–	–	–	34	–	–	34	–	34
– remeasurement of defined benefit asset/liability	–	–	(207)	–	–	–	–	(207)	–	(207)
– exchange differences	–	–	–	(1)	–	2	–	1	–	1
Total comprehensive income for the year	–	–	305	(5)	34	2	–	336	4	340
Capital securities issued	–	–	–	–	–	–	–	–	–	–
Dividends to shareholders	–	–	(451)	–	–	–	–	(451)	(4)	(455)
Capital contribution	–	–	–	–	–	–	–	–	–	–
Transfer	–	–	–	–	–	–	–	–	–	–
Group Reorganisation Reserve	–	–	–	–	–	–	–	–	–	–
Other movements[1]	–	–	33	–	–	–	–	33	–	33
At 31 Dec 2019	**9,015**	**2,196**	**3,292**	**9**	**(12)**	**–**	**7,691**	**22,191**	**60**	**22,251**
At 1 Jan 2018	15	–	–	–	–	–	–	15	–	15
Profit for the year	–	–	763	–	–	–	–	763	–	763
Other comprehensive income (net of tax)	–	–	(364)	10	(17)	(2)	–	(373)	–	(373)
– debt instruments at fair value through other comprehensive income	–	–	–	10	–	–	–	10	–	10
– cash flow hedges	–	–	–	–	(17)	–	–	(17)	–	(17)
– remeasurement of defined benefit asset/liability	–	–	(364)	–	–	–	–	(364)	–	(364)
– exchange differences	–	–	–	–	–	(2)	–	(2)	–	(2)
Total comprehensive income for the year	–	–	399	10	(17)	(2)	–	390	–	390
Capital securities issued[2]	9,000	–	–	–	–	–	–	9,000	–	9,000
Dividends to shareholders	–	–	–	–	–	–	–	–	(1)	(1)
Capital contribution[3]	–	–	3,000	–	–	–	–	3,000	–	3,000
Transfer[4,5]	–	2,196	–	–	–	–	–	2,196	60	2,256
Group Reorganisation Reserve[6]	–	–	–	4	(29)	–	7,691	7,666	–	7,666
Other movements	–	–	6	–	–	–	–	6	1	7
At 31 Dec 2018	9,015	2,196	3,405	14	(46)	(2)	7,691	22,273	60	22,333

1 *Relates primarily to £33m pension assets transfer from HSBC Global Services (UK) Limited in 2019 (2018: Nil).*
2 *All new capital subscribed during 2018 was issued to HSBC UK Holdings Limited.*
3 *HSBC UK Holdings Limited injected £3,000m of CET1 capital in 2018.*
4 *Other equity instruments amounting to £2,196m consists of additional Tier 1 capital issued during 2018.*
5 *Non-controlling interests ('NCI') of £60m transferred to the group relates to Marks and Spencer Financial Services plc.*
6 *Relates primarily to the recognition of goodwill £3,142m and the pension asset net of deferred tax £4,776m for the transfer of the ring- fenced businesses to HSBC UK Bank plc in 2018.*

HSBC UK Bank plc balance sheet

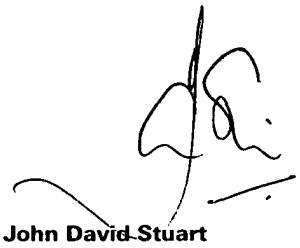
at 31 December

	Notes	2019 £m	2018 £m
Assets			
Cash and balances at central banks		**37,020**	33,187
Items in the course of collection from other banks		**355**	457
Financial assets designated and otherwise mandatorily measured at fair value through profit or loss	7	**66**	35
Derivatives	9	**118**	61
Loans and advances to banks		**4,643**	3,883
Loans and advances to customers		**173,901**	165,850
Reverse repurchase agreements – non-trading		**3,014**	3,422
Financial investments	10	**19,737**	13,203
Investments in subsidiaries	13	**1,600**	1,907
Prepayments, accrued income and other assets	16	**8,216**	8,523
Interests in joint ventures	12	**5**	5
Goodwill and intangible assets	15	**881**	718
Total assets		**249,556**	231,251
Liabilities and equity			
Liabilities			
Deposits by banks		**4,277**	4,265
Customer accounts		**207,830**	196,858
Repurchase agreements – non-trading		**98**	639
Items in the course of transmission to other banks		**336**	225
Derivatives	9	**197**	341
Debt securities in issue	17	**2,917**	–
Accruals, deferred income and other liabilities	18	**2,271**	2,274
Current tax liabilities		**362**	286
Provisions	19	**1,114**	515
Deferred tax liabilities	5	**1,255**	1,224
Subordinated liabilities	20	**9,454**	4,858
Total liabilities		**230,111**	211,485
Equity			
Called up share capital	23	**–**	–
Share premium account	23	**9,015**	9,015
Other equity instruments	23	**2,196**	2,196
Other reserves		**5,245**	5,214
Retained earnings		**2,989**	3,341
Total equity		**19,445**	19,766
Total liabilities and equity		**249,556**	231,251

Profit after tax for the year was £273m (2018: £701m)

The accompanying notes on pages 78 to 118, and the audited sections of the 'Report of the Directors' on pages 17 to 60 form an integral part of these financial statements.

These financial statements were approved by the Board of Directors on 17 February 2020 and signed on its behalf by:



John David Stuart

Director

HSBC UK Bank plc statement of cash flows

for the year ended 31 December

	2019	2018
	£m	£m
Profit before tax	**715**	968
Adjustments for non-cash items:		
Depreciation and amortisation[1]	**289**	94
Net loss from investing activities	**435**	—
Change in expected credit losses gross of recoveries and other credit impairment charges	**537**	313
Provisions including pensions	**1,005**	124
Share-based payment expense	**14**	(1)
Elimination of exchange differences[2]	**255**	(190)
Changes in operating assets and liabilities		
Change in net trading securities and derivatives	**(162)**	6
Change in loans and advances to banks and customers	**(8,392)**	(9,560)
Change in reverse repurchase agreements – non-trading	**408**	(3,422)
Change in financial assets designated and otherwise mandatorily measured at fair value	**(31)**	(27)
Change in other assets	**322**	1,801
Change in deposits by banks and customer accounts	**10,984**	5,457
Change in repurchase agreements – non-trading	**(541)**	639
Change in debt securities in issue	**2,917**	—
Change in other liabilities	**(875)**	(3,392)
Contributions paid to defined benefit plans	**(115)**	(80)
Tax paid	**(286)**	—
Net cash from operating activities	**7,479**	(7,270)
Purchase of financial investments	**(19,300)**	(5,369)
Proceeds from the sale and maturity of financial investments	**12,629**	3,290
Net cash flows from the purchase and sale of property, plant and equipment	**(50)**	(48)
Net investment in intangible assets	**(306)**	(154)
Net cash outflow on cost of investment in subsidiaries	**—**	(48)
Net cash flow on acquisition of subsidiaries, businesses and joint venture[3]	**—**	29,222
Net cash from investing activities	**(7,027)**	26,893
Issue of ordinary share capital and other equity instruments	**—**	9,000
Subordinated loan capital issued[4]	**4,619**	2,020
Funds received from the shareholder of the parent company	**—**	3,000
Dividends paid to shareholders of the parent company	**(451)**	—
Net cash from financing activities	**4,168**	14,020
Net increase in cash and cash equivalents	**4,620**	33,643
Cash and cash equivalents at 1 Jan	**33,673**	2
Exchange differences in respect of cash and cash equivalents	**(145)**	28
Cash and cash equivalents at 31 Dec[5]	**38,148**	33,673
Cash and cash equivalents comprise:		
– cash and balances at central banks	**37,020**	33,187
– items in the course of collection from other banks	**355**	457
– loans and advances to banks of one month or less	**1,001**	105
– treasury bills, other bills and certificates of deposit less than three months	**23**	149
– cash collateral and net settlement accounts	**85**	—
– less: items in the course of transmission to other banks	**(336)**	(225)
Cash and cash equivalents at 31 Dec[5]	**38,148**	33,673

Interest received was £5,183m (2018: £2,454m), interest paid was £971m (2018: £212m).

1 *The impact of the right-of-use assets recognised under IFRS 16 at the beginning of 2019 is not recognised in 2018.*
2 *Adjustment to bring changes between opening and closing balance sheet amounts to average rates. This is not done on line-by-line basis, as details cannot be determined without unreasonable expense.*
3 *No cash or cash equivalent was paid in consideration of the investment in subsidiaries and joint venture as it formed part of the Part VII transfer of asset and liabilities. The aggregate amount of cash and cash equivalent in the businesses over which control was obtained was £29,222m.*
4 *Subordinated liabilities changes during the year are attributable to cash flows from issuance of securities of £4,619m, (2018: £2,020m). Non-cash changes during the year included foreign exchange (loss) of £(23)m (2018: Nil).*
5 *At 31 December 2019, £617m (2018: £350m) was not available for use by the bank, all related to mandatory deposits at central banks (2018: £350m).*

HSBC UK Bank plc statement of changes in equity

for the year ended 31 December

	Called up share capital and share premium	Other equity instruments	Retained earnings	Other reserves: Financial assets at FVOCI reserve	Other reserves: Cash flow hedging reserve	Other reserves: Foreign exchange reserve	Other reserves: Group re-organisation reserve	Total share-holders' equity
	£m	£m	£m	£m	£m	£m	£m	£m
At 1 Jan 2019	**9,015**	**2,196**	**3,341**	**14**	**(46)**	**(2)**	**5,248**	**19,766**
Profit for the year	–	–	**273**	–	–	–	–	**273**
Other comprehensive income (net of tax)	–	–	**(207)**	**(5)**	**34**	**2**	–	**(176)**
– debt instruments at fair value through other comprehensive income	–	–	–	**(4)**	–	–	–	**(4)**
– cash flow hedges	–	–	–	–	**34**	–	–	**34**
– remeasurement of defined benefit asset/liability	–	–	**(207)**	–	–	–	–	**(207)**
– exchange differences	–	–	–	**(1)**	–	**2**	–	**1**
Total comprehensive income for the year	–	–	**66**	**(5)**	**34**	**2**	–	**97**
Capital securities issued	–	–	–	–	–	–	–	–
Dividends to shareholders	–	–	**(451)**	–	–	–	–	**(451)**
Capital contribution	–	–	–	–	–	–	–	–
Transfer	–	–	–	–	–	–	–	–
Group Reorganisation Reserve	–	–	–	–	–	–	–	–
Other movements[1]	–	–	**33**	–	–	–	–	**33**
At 31 Dec 2019	**9,015**	**2,196**	**2,989**	**9**	**(12)**	**–**	**5,248**	**19,445**
At 1 Jan 2018	15	–	–	–	–	–	–	15
Profit for the year	–	–	701	–	–	–	–	701
Other comprehensive income (net of tax)	–	–	(364)	10	(17)	(2)	–	(373)
– debt instruments at fair value through other comprehensive income	–	–	–	10	–	–	–	10
– cash flow hedges	–	–	–	–	(17)	–	–	(17)
– remeasurement of defined benefit asset/liability	–	–	(364)	–	–	–	–	(364)
– exchange differences	–	–	–	–	–	(2)	–	(2)
Total comprehensive income for the year	–	–	337	10	(17)	(2)	–	328
Capital securities issued[2]	9,000	–	–	–	–	–	–	9,000
Dividends to shareholders	–	–	–	–	–	–	–	–
Capital contribution[3]	–	–	3,000	–	–	–	–	3,000
Transfer[4]	–	2,196	–	–	–	–	–	2,196
Group Reorganisation Reserve[5]	–	–	–	4	(29)	–	5,248	5,223
Other movements	–	–	4	–	–	–	–	4
At 31 Dec 2018	9,015	2,196	3,341	14	(46)	(2)	5,248	19,766

1 *Relates primarily to £33m pension assets transfer from HSBC Global Services (UK) Limited in 2019 (2018: Nil).*
2 *All new capital subscribed during 2018 was issued to HSBC UK Holdings Limited.*
3 *HSBC UK Holdings Limited injected £3,000m of CET1 capital in 2018.*
4 *Other equity instruments amounting to £2,196m consists of additional Tier 1 capital issued during 2018.*
5 *Relates primarily to the recognition of the pension asset net of deferred tax £4,776m for the transfer of the ring- fenced businesses to HSBC UK Bank plc in 2018.*

Notes on the financial statements

1 Basis of preparation and significant accounting policies

1.1 Basis of preparation

(a) Compliance with International Financial Reporting Standards

The consolidated financial statements of HSBC UK and the separate financial statements of the bank have been prepared in accordance with International Financial Reporting Standards ('IFRSs') as issued by the International Accounting Standards Board ('IASB'), including interpretations issued by the IFRS Interpretations Committee, and as endorsed by the European Union ('EU'). 'Interest Rate Benchmark Reform: Amendments to IFRS 9 and IAS 39 'Financial Instruments', was endorsed in January 2020 and has been early adopted as set out below. Therefore, there were no unendorsed standards effective for the year ended 31 December 2019 affecting these consolidated and separate financial statements, and the group's application of IFRSs results in no differences between IFRSs as issued by the IASB and IFRSs as endorsed by the EU.

Standards adopted during the year ended 31 December 2019

IFRS 16 'Leases'

On 1 January 2019, we adopted the requirements of IFRS 16 retrospectively. The cumulative effect of initially applying the standard was recognised as an adjustment to the opening balance of retained earnings at that date. Comparatives were not restated. The adoption of the standard increased assets by £0.4bn and increased financial liabilities by the same amount with no effect on net assets or retained earnings.

On adoption of IFRS 16, we recognised lease liabilities in relation to leases that had previously been classified as 'operating leases' in accordance with IAS 17 'Leases'. These liabilities were recognised in 'other liabilities' and measured at the present value of the remaining lease payments, discounted at the lessee's incremental borrowing rate at 1 January 2019. The associated right of use ('ROU') assets were recognised in 'other assets' and measured at the amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments or provisions for onerous leases recognised on the balance sheet at 31 December 2018. In addition, the following practical expedients permitted by the standard were applied:

- reliance was placed on previous assessments on whether leases were onerous;
- operating leases with a remaining lease term of less than 12 months at 1 January 2019 were treated as short-term leases; and
- initial direct costs were not included in the measurement of ROU assets for leases previously accounted for as operating leases.

The differences between IAS 17 and IFRS 16 are summarised in the table below:

IAS 17	IFRS 16
Leases were classified as either finance or operating leases. Payments made under operating leases were charged to profit or loss on a straight-line basis over the period of the lease.	Leases are recognised as an ROU asset and a corresponding liability at the date at which the leased asset is made available for use. Lease payments are allocated between the liability and finance cost. The finance cost is charged to profit or loss over the lease term so as to produce a constant period rate of interest on the remaining balance of the liability. The ROU asset is depreciated over the shorter of the ROU asset's useful economic life and the lease term on a straight-line basis. In determining the lease term, we consider all facts and circumstances that create an economic incentive to exercise an extension option or not exercise a termination option over the planning horizon of five years. In general, it is not expected that the discount rate implicit in the lease is available so the lessee's incremental borrowing rate is used. This is the rate that the lessee would have to pay to borrow the funds necessary to obtain an asset of a similar value in a similar economic environment with similar terms and conditions. The rates are determined for each economic environment in which we operate and for each term by adjusting swap rates with funding spreads (own credit spread) and cross-currency basis where appropriate.

Interest Rate Benchmark Reform: Amendments to IFRS 9 and IAS 39 'Financial Instruments'

Amendments to IFRS 9 and IAS 39 issued in September 2019 modify specific hedge accounting requirements so that entities apply those hedge accounting requirements assuming that the interest rate benchmark on which the hedged cash flows and cash flows of the hedging instrument are based is not altered as a result of interest rate benchmark reform. These amendments replace the need for specific judgements to determine whether certain hedge accounting relationships that hedge the variability of cash flows or interest rate risk exposures for periods after the interest rate benchmarks are expected to be reformed or replaced continue to qualify for hedge accounting as at 31 December 2019. For example, in the context of cash flow hedging, the amendments require the interest rate benchmark on which the hedged cash flows are based, or on which the cash flows of the hedging instrument are based, to be assumed to be unaltered over the period of the documented hedge relationship, while uncertainty over the interest rate benchmark reform exists. The IASB is expected to provide further guidance on the implication for hedge accounting during the reform process and after the reform uncertainty is resolved.

These amendments apply from 1 January 2020 with early adoption permitted. The group has adopted the amendments that apply to IAS 39 from 1 January 2019 and has made the additional disclosures as required by the amendments. Further information is included in Note 9.

Amendment to IAS 12 'Income Taxes' and other changes

An amendment to IAS 12 was issued in December 2017 as part of the annual improvement cycle. The amendment clarifies that an entity should recognise the tax consequences of dividends where the transactions or events that generated the distributable profits are recognised. This amendment was applied on 1 January 2019 and had no material impact. Comparatives have not been restated.

In addition, the group has adopted a number of interpretations and amendments to standards, which have had an insignificant effect on the consolidated group and the separate financial statements of the bank.

(b) Future accounting developments

Minor amendments to IFRSs

The IASB has published a number of minor amendments to IFRSs which are effective from 1 January 2020, some of which have been endorsed for use in the EU. The group expects they will have an insignificant effect, when adopted, on the consolidated financial statements of the group and the separate financial statements of the bank.

Major new IFRSs

The IASB has published IFRS 17 'Insurance Contracts'. IFRS 17 has not yet been endorsed but is not expected to have a significant impact on the consolidated financial statements of the group and the separate financial statements of the bank.

(c) Foreign currencies

The functional currency of the bank is sterling, which is also the presentational currency of the consolidated financial statements of the group.

Transactions in foreign currencies are recorded at the rate of exchange on the date of the transaction. Assets and liabilities denominated in foreign currencies are translated at the rate of exchange at the balance sheet date except non-monetary assets and liabilities measured at historical cost, which are translated using the rate of exchange at the initial transaction date. Exchange differences are included in other comprehensive income or in the income statement depending on where the gain or loss on the underlying item is recognised.

(d) Presentation of information

Certain disclosures required by IFRSs have been included in the audited sections of this *Annual Report and Accounts 2019* as follows:

- disclosures concerning the nature and extent of risks relating to financial instruments are included in the 'Report of the Directors: Risk' on pages 17 to 51; and
- capital disclosures are included in the 'Report of the Directors: Capital' on pages 52 to 53.

In publishing the parent company financial statements together with the group financial statements, the bank has taken advantage of the exemption in Section 408(3) of the Companies Act 2006 not to present its individual income statement and related notes.

(e) Critical accounting estimates and judgements

The preparation of financial information requires the use of estimates and judgements about future conditions. In view of the inherent uncertainties and the high level of subjectivity involved in the recognition or measurement of items highlighted as the critical accounting estimates and judgements in section 1.2 below, it is possible that the outcomes in the next financial year could differ from those on which management's estimates are based. This could result in materially different estimates and judgements from those reached by management for the purposes of these financial statements. Management's selection of the group's accounting policies that contain critical estimates and judgements reflects the materiality of the items to which the policies are applied and the high degree of judgement and estimation uncertainty involved.

(f) Segmental analysis

HSBC UK's chief operating decision-maker is the group Chief Executive, supported by the group Executive Committee, and operating segments are reported in a manner consistent with the internal reporting provided to the group Chief Executive and the group Executive Committee.

Measurement of segmental assets, liabilities, income and expenses is in accordance with the group's accounting policies. Segmental income and expenses include transfers between segments and these transfers are conducted at arm's length. Shared costs are included in segments on the basis of the actual recharges made.

The types of products and services from which each reportable segment derives its revenue are discussed in the 'Strategic Report – Products and services'.

(g) Going concern

The financial statements are prepared on a going concern basis, as the Directors are satisfied that the group and bank have the resources to continue in business for the foreseeable future. In making this assessment, the Directors have considered a wide range of information relating to present and future conditions, including future projections of profitability, cash flows and capital resources.

1.2 Summary of significant accounting policies

(a) Consolidation and related policies

Investments in subsidiaries

Where an entity is governed by voting rights, the group consolidates when it holds, directly or indirectly, the necessary voting rights to pass resolutions by the governing body. In all other cases, the assessment of control is more complex and requires judgement of other factors, including having exposure to variability of returns, power to direct relevant activities and whether power is held as agent or principal.

Business combinations are accounted for using the acquisition method. The amount of non-controlling interest is measured either at fair value or at the non-controlling interest's proportionate share of the acquiree's identifiable net assets. The election is made for each business combination.

The bank's investments in subsidiaries are stated at cost less impairment losses.

Goodwill

Goodwill is allocated to cash-generating units ('CGUs') for the purpose of impairment testing, which is undertaken at the lowest level at which goodwill is monitored for internal management purposes. The group's CGUs are based on the business lines described in the Strategic Report. Impairment testing is performed once a year, or whenever there is an indication of impairment, by comparing the recoverable amount of a CGU with its carrying amount.

Goodwill is included in a disposal group if the disposal group is a CGU to which goodwill has been allocated or it is an operation within such a CGU. The amount of goodwill included in a disposal group is measured on the basis of the relative values of the operation disposed of and the portion of the CGU retained.

Critical accounting estimates and judgements

The review of goodwill for impairment reflects management's best estimate of the future cash flows of the CGUs and the rates used to discount these cash flows, both of which are subject to uncertain factors as follows:

Judgements	Estimates
• The accuracy of forecast cash flows is subject to a high degree of uncertainty in volatile market conditions. Where such circumstances are determined to exist, management re-tests goodwill for impairment more frequently than once a year when indicators of impairment exist. This ensures that the assumptions on which the cash flow forecasts are based continue to reflect current market conditions and management's best estimate of future business prospects	• The future cash flows of the CGUs are sensitive to the cash flows projected for the periods for which detailed forecasts are available and to assumptions regarding the long-term pattern of sustainable cash flows thereafter. Forecasts are compared with actual performance and verifiable economic data, but they reflect management's view of future business prospects at the time of the assessment • The rates used to discount future expected cash flows can have a significant effect on their valuation, and are based on the costs of capital assigned to individual CGUs. The cost of capital percentage is generally derived from a capital asset pricing model, which incorporates inputs reflecting a number of financial and economic variables, including the risk-free interest rate in the country concerned and a premium for the risk of the business being evaluated. These variables are subject to fluctuations in external market rates and economic conditions beyond management's control • Key assumptions used in estimating goodwill impairment are described in Note 15

Interests in associates and joint arrangements

Joint arrangements are investments in which the group, together with one or more parties, has joint control. Depending on the group's rights and obligations, the joint arrangement is classified as either a joint operation or a joint venture. The group classifies investments in entities over which it has significant influence, and that are neither subsidiaries nor joint arrangements, as associates.

The group recognises its share of the assets, liabilities and results in a joint operation. Investments in associates and interests in joint ventures are recognised using the equity method. The attributable share of the results and reserves of joint ventures and associates are included in the consolidated financial statements of the group based on either financial statements made up to 31 December or pro-rated amounts adjusted for any material transactions or events occurring between the date the financial statements are available and 31 December.

Investments in associates and joint ventures are assessed at each reporting date and tested for impairment when there is an indication that the investment may be impaired. Goodwill on acquisition of interests in joint ventures and associates is not tested separately for impairment, but is assessed as part of the carrying amount of the investment.

(b) Income and expense

Operating income

Interest income and expense

Interest income and expense for all financial instruments, excluding those classified as held for trading or designated at fair value, are recognised in 'Interest income' and 'Interest expense' in the income statement using the effective interest method. However, as an exception to this, interest on debt instruments issued by the group for funding purposes that are designated under the fair value option to reduce an accounting mismatch and on derivatives managed in conjunction with those debt instruments is included in interest expense.

Interest on credit-impaired financial assets is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

Critical accounting estimates and judgements

The effective interest rate applied to interest income recognised on credit card lending includes significant estimates and judgements related to their behavioural life. This life is estimated based on internal models and is reviewed regularly to reflect actual experience. The application of the effective interest rate method to credit card lending has resulted in the recognition of £147m (2018: £138m) within loans and advances to customers as at 31 December 2019.

Judgements	Estimates
• The estimated life is reviewed annually and management has assessed seven years as continuing to be the most appropriate life. • A key metric is the stick rate, being the proportion of acquired balances which remain on book after the end of promotional period. Where actual experience differs from forecasts, an adjustment to the carrying value of the asset is required to be recognised in the financial statements.	Management has assessed the sensitivity of balance and interest assumptions by considering the impact of changes as follows: • a decrease in the closing balance stick rate assumption of 5% would decrease the asset value by £7.7m (2018:£3.8m); • similarly, a decrease in the assumed interest yield of 5% would decrease the asset value by £17.0m (2018: £14.6m). (The interest yield assumption is the amount of interest receivable over the life of the account).

Non-interest income and expense

The group generates fee income from services provided at a fixed price over time, such as account service and card fees, or when it delivers a specific transaction at a point in time, such as broking services and import/export services. With the exception of certain performance fees, all other fees are generated at a fixed price. Fund management and performance fees can be variable depending on the size of the customer portfolio and the group's performance as fund manager. Variable fees are recognised when all uncertainties are resolved. Fee income is generally earned from short-term contracts with payment terms that do not include a significant financing component.

The group acts as principal in the majority of contracts with customers, with the exception of broking services. For most brokerage trades, the group acts as agent in the transaction and recognises broking income net of fees payable to other parties in the arrangement.

The group recognises fees earned on transaction-based arrangements at a point in time when it has fully provided the service to the customer. Where the contract requires services to be provided over time, income is recognised on a systematic basis over the life of the agreement.

Where the group offers a package of services that contains multiple non-distinct performance obligations, such as those included in account service packages, the promised services are treated as a single performance obligation. If a package of services contains distinct performance obligations, such as those including both account and insurance services, the corresponding transaction price is allocated to each performance obligation based on the estimated stand-alone selling prices.

Dividend income is recognised when the right to receive payment is established. This is the ex-dividend date for listed equity securities, and usually the date when shareholders approve the dividend for unlisted equity securities.

The group buys and sells currencies to customers, as principal and presents the results of this activity, including the related gains and losses from changes in foreign exchange rates, as trading.

Net income/(expense) from financial instruments measured at fair value through profit or loss includes the following:

- 'Net income from financial instruments held for trading or managed on a fair value basis': This comprises net trading income, which includes all gains and losses from changes in the fair value of financial assets and financial liabilities held for trading and other financial instruments managed on a fair value basis, together with the related interest income, expense and dividends, excluding the effect of changes in the credit risk of liabilities managed on a fair value basis. It also includes all gains and losses from changes in the fair value of derivatives that are managed in conjunction with financial assets and liabilities measured at fair value through profit or loss.
- 'Changes in fair value of other financial instruments mandatorily measured at fair value through profit or loss': This includes interest on instruments that fail the solely payments of principal and interest ('SPPI') test, see (d).

(c) Valuation of financial instruments

All financial instruments are initially recognised at fair value. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value of a financial instrument on initial recognition is generally its transaction price (that is, the fair value of the consideration given or received). However, if there is a difference between the transaction price and the fair value of financial instruments whose fair value is based on a quoted price in an active market or a valuation technique that uses only data from observable markets, the group recognises the difference as a trading gain or loss at inception (a 'day 1 gain or loss'). In all other cases, the entire day 1 gain or loss is deferred and recognised in the income statement over the life of the transaction either until the transaction matures or is closed out or the valuation inputs become observable.

The fair value of financial instruments is generally measured on an individual basis. Financial instruments are classified into one of three fair value hierarchy levels, described in Note 7, 'Fair values of financial instruments carried at fair value'.

(d) Financial instruments measured at amortised cost

Financial assets that are held to collect the contractual cash flows and which contain contractual terms that give rise on specified dates to cash flows that are solely payments of principal and interest are measured at amortised cost. Such financial assets include most loans and advances to banks and customers and some debt securities. In addition, most financial liabilities are measured at amortised cost. The group accounts for regular way amortised cost financial instruments using trade date accounting. The carrying value of these financial assets at initial recognition includes any directly attributable transactions costs. If the initial fair value is lower than the cash amount advanced, such as in the case of some leveraged finance and syndicated lending activities, the difference is deferred and recognised over the life of the loan through the recognition of interest income.

Non-trading reverse repurchase, repurchase and similar agreements

When debt securities are sold subject to a commitment to repurchase them at a predetermined price ('repos'), they remain on the balance sheet and a liability is recorded in respect of the consideration received. Securities purchased under commitments to resell ('reverse repos') are not recognised on the balance sheet and an asset is recorded in respect of the initial consideration paid. Non-trading repos and reverse repos are measured at amortised cost. The difference between the sale and repurchase price or between the purchase and resale price is treated as interest and recognised in net interest income over the life of the agreement.

(e) Financial assets measured at fair value through other comprehensive income

Financial assets held for a business model that is achieved by both collecting contractual cash flows and selling and which contain contractual terms that give rise on specified dates to cash flows that are solely payments of principal and interest are measured at fair value through other comprehensive income ('FVOCI'). These comprise primarily debt securities. They are recognised on the trade date when the group enters into contractual arrangements to purchase and are normally derecognised when they are either sold or redeemed. They are subsequently remeasured at fair value and changes therein (except for those relating to impairment, interest income and foreign currency exchange gains and losses) are recognised in other comprehensive income until the assets are sold. Upon disposal, the cumulative gains or losses in other comprehensive income are recognised in the income statement as 'Gains less losses from financial instruments'. Financial assets measured at FVOCI are included in the impairment calculations set out below and impairment is recognised in profit or loss.

(f) Derivatives

Derivatives are financial instruments that derive their value from the price of underlying items such as equities, interest rates or other indices. Derivatives are recognised initially and are subsequently measured at fair value through profit or loss. Derivatives are classified as assets when their fair value is positive or as liabilities when their fair value is negative. This includes embedded derivatives in financial liabilities, which are bifurcated from the host contract when they meet the definition of a derivative on a stand-alone basis.

Where the derivatives are managed with debt securities issued by the group that are designated at fair value, the contractual interest is shown in 'Interest expense' together with the interest payable on the issued debt.

Hedge accounting

When derivatives are not part of fair value designated relationships, if held for risk management purposes they are designated in hedge accounting relationships where the required criteria for documentation and hedge effectiveness are met. The group uses these derivatives or, where allowed, other non-derivative hedging instruments in fair value hedges or cash flow hedges as appropriate to the risk being hedged.

Fair value hedge

Fair value hedge accounting does not change the recording of gains and losses on derivatives and other hedging instruments, but results in recognising changes in the fair value of the hedged assets or liabilities attributable to the hedged risk that would not otherwise be recognised in the income statement. If a hedge relationship no longer meets the criteria for hedge accounting, hedge accounting is discontinued and the cumulative adjustment to the carrying amount of the hedged item is amortised to the income statement on a recalculated effective interest rate, unless the hedged item has been derecognised, in which case it is recognised in the income statement immediately.

Cash flow hedge

The effective portion of gains and losses on hedging instruments is recognised in other comprehensive income and the ineffective portion of the change in fair value of derivative hedging instruments that are part of a cash flow hedge relationship is recognised immediately in the income statement within 'Net income from financial instruments held for trading or managed on a fair value basis'. The accumulated gains and losses recognised in other comprehensive income are reclassified to the income statement in the same periods in which the hedged item affects profit or loss. When a hedge relationship is discontinued, or partially discontinued, any cumulative gain or loss recognised in other comprehensive income remains in equity until the forecast transaction is recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss previously recognised in other comprehensive income is immediately reclassified to the income statement.

(g) Impairment of amortised cost and FVOCI financial assets

Expected credit losses ('ECL') are recognised for loans and advances to banks and customers, non-trading reverse repurchase agreements, other financial assets held at amortised cost, debt instruments measured at FVOCI, and certain loan commitments and financial guarantee contracts. At initial recognition, allowance (or provision in the case of some loan commitments and financial guarantees) is required for ECL resulting from default events that are possible within the next 12 months, or less, where the remaining life is less than 12 months ('12-month ECL'). In the event of a significant increase in credit risk, allowance (or provision) is required for ECL resulting from all possible default events over the expected life of the financial instrument ('lifetime ECL'). Financial assets where 12-month ECL is recognised are considered to be 'stage 1'; financial assets which are considered to have experienced a significant increase in credit risk are in 'stage 2'; and financial assets for which there is objective evidence of impairment so are considered to be in default or otherwise credit impaired are in 'stage 3'. Purchased or originated credit-impaired financial assets ('POCI') are treated differently, as set out below.

Credit impaired (stage 3)

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

- contractual payments of either principal or interest are past due for more than 90 days;
- there are other indications that the borrower is unlikely to pay, such as when a concession has been granted to the borrower for economic or legal reasons relating to the borrower's financial condition; and
- the loan is otherwise considered to be in default.

If such unlikeliness to pay is not identified at an earlier stage, it is deemed to occur when an exposure is 90 days past due, even where regulatory rules permit default to be defined based on 180 days past due. Therefore, the definitions of credit impaired and default are aligned as far as possible so that stage 3 represents all loans that are considered defaulted or otherwise credit impaired.

Interest income is recognised by applying the effective interest rate to the amortised cost amount, i.e. gross carrying amount less ECL allowance.

Write-off

Financial assets (and the related impairment allowances) are normally written off, either partially or in full, when there is no realistic prospect of recovery. Where loans are secured, this is generally after receipt of any proceeds from the realisation of security. In circumstances where the net realisable value of any collateral has been determined and there is no reasonable expectation of further recovery, write-off may be earlier.

Renegotiation

Loans are identified as renegotiated and classified as credit impaired when we modify the contractual payment terms due to significant credit distress of the borrower. Renegotiated loans remain classified as credit impaired until there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows and retain the designation of renegotiated until maturity or derecognition.

A loan that is renegotiated is derecognised if the existing agreement is cancelled and a new agreement is made on substantially different terms or if the terms of an existing agreement are modified such that the renegotiated loan is a substantially different financial instrument. Any new loans that arise following derecognition events in these circumstances are considered to be POCI and will continue to be disclosed as renegotiated loans.

Other than originated credit-impaired loans, all other modified loans could be transferred out of stage 3 if they no longer exhibit any evidence of being credit impaired and, in the case of renegotiated loans, there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows over the minimum observation period, and there are no other indicators of impairment. These loans could be transferred to stage 1 or 2 based on the mechanism as described below by comparing the risk of a default occurring at the reporting date (based on the modified contractual terms) and the risk of a default occurring at initial recognition (based on the original, unmodified contractual terms). Any amount written off as a result of the modification of contractual terms would not be reversed.

Loan modifications that are not credit impaired

Loan modifications that are not identified as renegotiated are considered to be commercial restructuring. Where a commercial restructuring results in a modification (whether legalised through an amendment to the existing terms or the issuance of a new loan contract) such that the group's rights to the cash flows under the original contract have expired, the old loan is derecognised and the new loan is recognised at fair value. The rights to cash flows are generally considered to have expired if the commercial restructure is at

market rates and no payment-related concession has been provided.

Significant increase in credit risk (stage 2)

An assessment of whether credit risk has increased significantly since initial recognition is performed at each reporting period by considering the change in the risk of default occurring over the remaining life of the financial instrument. The assessment explicitly or implicitly compares the risk of default occurring at the reporting date with that at initial recognition, taking into account reasonable and supportable information, including information about past events, current conditions and future economic conditions. The assessment is unbiased, probability-weighted, and to the extent relevant, uses forward-looking information consistent with that used in the measurement of ECL. The analysis of credit risk is multifactor. The determination of whether a specific factor is relevant and its weight compared with other factors depends on the type of product, the characteristics of the financial instrument and the borrower. Therefore, it is not possible to provide a single set of criteria that will determine what is considered to be a significant increase in credit risk and these criteria will differ for different types of lending, particularly between retail and wholesale. However, unless identified at an earlier stage, all financial assets are deemed to have suffered a significant increase in credit risk when 30 days past due. In addition, wholesale loans that are individually assessed, which are typically corporate and commercial customers, and included on a watch or worry list, are included in stage 2.

For wholesale portfolios, the quantitative comparison assesses default risk using a lifetime probability of default ('PD'), which encompasses a wide range of information including the obligor's customer risk rating ('CRR'), macroeconomic condition forecasts and credit transition probabilities. For origination CRRs up to 3.3, significant increase in credit risk is measured by comparing the average PD for the remaining term estimated at origination with the equivalent estimation at the reporting date. The quantitative measure of significance varies depending on the credit quality at origination as follows:

Origination CRR	Significance trigger – PD to increase by
0.1-1.2	15bps
2.1-3.3	30 bps

For CRRs greater than 3.3 that are not impaired, a significant increase in credit risk is considered to have occurred when the origination PD has doubled. The significance of changes in PD was informed by expert credit risk judgement, referenced to historical credit migrations and to relative changes in external market rates.

For loans originated prior to the implementation of IFRS 9, the origination PD does not include adjustments to reflect expectations of future macroeconomic conditions since these are not available without the use of hindsight. In the absence of this data, origination PD must be approximated assuming through-the-cycle ('TTC') PDs and TTC migration probabilities, consistent with the instrument's underlying modelling approach and the CRR at origination. For these loans, the quantitative comparison is supplemented with additional CRR deterioration-based thresholds, as set out in the table below:

Origination CRR	Additional significance criteria – Number of CRR grade notches deterioration required to identify as significant credit deterioration (stage 2) (> or equal to)
0.1	5 notches
1.1-4.2	4 notches
4.3-5.1	3 notches
5.2-7.1	2 notches
7.2-8.2	1 notch
8.3	0 notch

Further information about the 23-grade scale used for CRR can be found on page 25 – Risk rating scales.

For certain portfolios of debt securities where external market ratings are available and credit ratings are not used in credit risk management, the debt securities will be in stage 2 if their credit risk increases to the extent they are no longer considered investment grade. Investment grade is where the financial instrument has a low risk of incurring losses, the structure has a strong capacity to meet its contractual cash flow obligations in the near term and adverse changes in economic and business conditions in the longer term may, but will not necessarily, reduce the ability of the borrower to fulfil their contractual cash flow obligations.

For retail portfolios, default risk is assessed using a reporting date 12-month PD derived from credit scores, which incorporates all available information about the customer. This PD is adjusted for the effect of macroeconomic forecasts for periods longer than 12 months and is considered to be a reasonable approximation of a lifetime PD measure. Retail exposures are first segmented into homogeneous portfolios, generally by country, product and brand. Within each portfolio, the stage 2 accounts are defined as accounts with an adjusted 12-month PD greater than the average 12-month PD of loans in that portfolio 12 months before they become 30 days past due. The expert credit risk judgement is that no prior increase in credit risk is significant. This portfolio-specific threshold identifies loans with a PD higher than would be expected from loans that are performing as originally expected, and higher than what would have been acceptable at origination. It therefore approximates a comparison of origination to reporting date PDs.

Unimpaired and without significant increase in credit risk (stage 1)

ECL resulting from default events that are possible within the next 12 months ('12-month ECL') are recognised for financial instruments that remain in stage 1.

Purchased or originated credit impaired

Financial assets that are purchased or originated at a deep discount that reflects the incurred credit losses are considered to be POCI. This population includes the recognition of a new financial instrument following a renegotiation where concessions have been granted for economic or contractual reasons relating to the borrower's financial difficulty that otherwise would not have been considered. The amount of change-in-lifetime ECL is recognised in profit or loss until the POCI is derecognised, even if the lifetime ECL are less than the amount of ECL included in the estimated cash flows on initial recognition.

Movement between stages

Financial assets can be transferred between the different categories (other than POCI) depending on their relative increase in credit risk since initial recognition. Financial instruments are transferred out of stage 2 if their credit risk is no longer considered to be significantly increased since initial recognition based on the assessments described above. Except for renegotiated loans, financial instruments are

transferred out of stage 3 when they no longer exhibit any evidence of credit impairment as described above. Renegotiated loans that are not POCI will continue to be in stage 3 until there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows, observed over a minimum one-year period and there are no other indicators of impairment. For loans that are assessed for impairment on a portfolio basis, the evidence typically comprises a history of payment performance against the original or revised terms, as appropriate to the circumstances. For loans that are assessed for impairment on an individual basis, all available evidence is assessed on a case-by-case basis.

Measurement of ECL

The assessment of credit risk and the estimation of ECL are unbiased and probability-weighted, and incorporate all available information that is relevant to the assessment including information about past events, current conditions and reasonable and supportable forecasts of future events and economic conditions at the reporting date. In addition, the estimation of ECL should take into account the time value of money.

In general, the group calculates ECL using three main components: a probability of default, a loss given default ('LGD') and the exposure at default ('EAD').

The 12-month ECL is calculated by multiplying the 12-month PD, LGD and EAD. Lifetime ECL is calculated using the lifetime PD instead. The 12-month and lifetime PDs represent the probability of default occurring over the next 12 months and the remaining maturity of the instrument respectively.

The EAD represents the expected balance at default, taking into account the repayment of principal and interest from the balance sheet date to the default event together with any expected drawdowns of committed facilities. The LGD represents expected losses on the EAD given the event of default, taking into account, among other attributes, the mitigating effect of collateral value at the time it is expected to be realised and the time value of money.

The group leverages the Basel II IRB framework where possible, with recalibration to meet the differing IFRS 9 requirements as set out in the following table:

Model	Regulatory capital	IFRS 9
PD	Through the cycle (represents long-run average PD throughout a full economic cycle).	Point in time (based on current conditions, adjusted to take into account estimates of future conditions that will impact PD).
	The definition of default includes a backstop of 90+ days past due, although this has been modified to 180+ days past due for some portfolios, particularly UK and US mortgages.	Default backstop of 90+ days past due for all portfolios.
EAD	Cannot be lower than current balance	Amortisation captured for term products
LGD	Downturn LGD (consistent losses expected to be suffered during a severe but plausible economic downturn).	Expected LGD (based on estimate of loss given default including the expected impact of future economic conditions such as changes in value of collateral).
	Regulatory floors may apply to mitigate risk of underestimating downturn LGD due to lack of historical data.	No floors.
	Discounted using cost of capital.	Discounted using the original effective interest rate of the loan.
	All collection costs included.	Only costs associated with obtaining/selling collateral included.
Other		Discounted back from point of default to balance sheet date.

While 12-month PDs are recalibrated from Basel II models where possible, the lifetime PDs are determined by projecting the 12-month PD using a term structure. For the wholesale methodology, the lifetime PD also takes into account credit migration, i.e. a customer migrating through the CRR bands over its life.

The ECL for wholesale stage 3 is determined on an individual basis using a discounted cash flow ('DCF') methodology. The expected future cash flows are based on the credit risk officer's estimates as at the reporting date, reflecting reasonable and supportable assumptions and projections of future recoveries and expected future receipts of interest. Collateral is taken into account if it is likely that the recovery of the outstanding amount will include realisation of collateral based on the estimated fair value of collateral at the time of expected realisation, less costs for obtaining and selling the collateral. The cash flows are discounted at a reasonable approximation of the original effective interest rate. For significant cases, cash flows under four different scenarios are probability-weighted by reference to the economic scenarios applied more generally by the group and the judgement of the credit risk officer in relation to the likelihood of the workout strategy succeeding or receivership being required. For less significant cases, the effect of different economic scenarios and work-out strategies is approximated and applied as an adjustment to the most likely outcome.

Period over which ECL is measured

Expected credit loss is measured from the initial recognition of the financial asset. The maximum period considered when measuring ECL (be it 12-month or lifetime ECL) is the maximum contractual period over which the group is exposed to credit risk. For wholesale overdrafts, credit risk management actions are taken no less frequently than on an annual basis and therefore this period is to the expected date of the next substantive credit review. The date of the substantive credit review also represents the initial recognition of the new facility. However, where the financial instrument includes both a drawn and undrawn commitment and the contractual ability to demand repayment and cancel the undrawn commitment does not serve to limit the group's exposure to credit risk to the contractual notice period, the contractual period does not determine the maximum period considered. Instead, ECL is measured over the period the group remains exposed to credit risk that is not mitigated by credit risk management actions. This applies to retail overdrafts and credit cards, where the period is the average time taken for stage 2 exposures to default or close as performing accounts, determined on a portfolio basis and ranging from between two and six years. In addition, for these facilities it is not possible to identify the ECL on the loan commitment component separately from the financial asset component. As a result, the total ECL is recognised in the loss allowance for the financial asset unless the total ECL exceeds the gross carrying amount of the financial asset, in which case the ECL is recognised as a provision.

Forward-looking economic inputs

The group applies multiple forward-looking global economic scenarios determined with reference to external forecast distributions representative of our view of forecast economic conditions. This approach is considered sufficient to calculate unbiased expected loss in

most economic environments. In certain economic environments, additional analysis and may be necessary and result in additional scenarios or adjustments, to reflect a range of possible economic outcomes sufficient for an unbiased estimate. The detailed methodology is disclosed in 'Measurement uncertainty and sensitivity analysis of ECL estimates' on page 31.

Critical accounting estimates and judgements

The calculation of the group's ECL under IFRS 9 requires the Group to make a number of judgements, assumptions and estimates. The most significant are set out below:

Judgements	Estimates
• Defining what is considered to be a significant increase in credit risk. • Determining the lifetime and point of initial recognition of overdrafts and credit cards. • Selecting and calibrating the PD, LGD and EAD models, which support the calculations, including making reasonable and supportable judgements about how models react to current and future economic conditions. • Selecting model inputs and economic forecasts, including determining whether sufficient and appropriately weighted economic forecasts are incorporated to calculate unbiased expected loss.	• The sections marked as audited on pages 31 to 34, 'Measurement uncertainty and sensitivity analysis of ECL estimates' set out the assumptions used in determining ECL and provide an indication of the sensitivity of the result to the application of different weightings being applied to different economic assumptions.

(h) Employee compensation and benefits

Share-based payments

The group enters into both equity-settled and cash-settled share-based payment arrangements with its employees as compensation for the provision of their services.

The vesting period for these schemes may commence before the legal grant date if the employees have started to render services in respect of the award before the legal grant date, where there is a shared understanding of the terms and conditions of the arrangement. Expenses are recognised when the employee starts to render service to which the award relates.

Cancellations result from the failure to meet a non-vesting condition during the vesting period, and are treated as an acceleration of vesting recognised immediately in the income statement. Failure to meet a vesting condition by the employee is not treated as a cancellation, and the amount of expense recognised for the award is adjusted to reflect the number of awards expected to vest.

Post-employment benefit plans

The group operates a pension plan which provides defined benefit and defined contribution pensions.

Payments to defined contribution schemes are charged as an expense as the employees render service.

Defined benefit pension obligations are calculated using the projected unit credit method. The net charge to the income statement mainly comprises the service cost and the net interest on the net defined benefit asset or liability, and is presented in operating expenses.

Remeasurements of the net defined benefit asset or liability, which comprise actuarial gains and losses, return on plan assets (excluding interest) and the effect of the asset ceiling (if any, excluding interest), are recognised immediately in other comprehensive income. The net defined benefit asset or liability represents the present value of defined benefit obligations reduced by the fair value of plan assets, after applying the asset ceiling test, where the net defined benefit surplus is limited to the present value of available refunds and reductions in future contributions to the plan.

The cost of obligations arising from other post-employment plans are accounted for on the same basis as defined benefit pension plans.

Critical accounting estimates and judgements

The most significant critical accounting judgements and estimates relate to the determination of key assumptions applied in calculating the defined benefit pension obligation.

Judgements	Estimates
	• A range of assumptions could be applied, and different assumptions could significantly alter the defined benefit obligation and the amounts recognised in profit or loss or OCI. • The calculation of the defined benefit pension obligation includes assumptions with regard to the discount rate, inflation rate, pension payments and deferred pensions, pay and mortality. Management determines these assumptions in consultation with the plan's actuaries. • Key assumptions used in calculating the defined benefit pension obligation and the sensitivity of the calculation to different assumptions are described in Note 3

(i) Tax

Income tax comprises current tax and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised in other comprehensive income or directly in equity, in which case the tax is recognised in the same statement in which the related item appears.

Current tax is the tax expected to be payable on the taxable profit for the year and on any adjustment to tax payable in respect of previous years. The group provides for potential current tax liabilities that may arise on the basis of the amounts expected to be paid to the tax authorities.

Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the balance sheet, and the amounts attributed to such assets and liabilities for tax purposes. Deferred tax is calculated using the tax rates expected to apply in the periods as the assets will be realised or the liabilities settled.

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

(j) Provisions, contingent liabilities and guarantees

Provisions

Provisions are recognised when it is probable that an outflow of economic benefits will be required to settle a present legal or constructive obligation that has arisen as a result of past events and for which a reliable estimate can be made.

Critical accounting estimates and judgements

The recognition and measurement of provisions requires the group to make a number of judgements, assumptions and estimates. The most significant are set out below:

Judgements	Estimates
• Determining whether a present obligation exists. Professional advice is taken on the assessment of litigation and similar obligations. • Provisions for legal proceedings and regulatory matters typically require a higher degree of judgement than other types of provisions. When matters are at an early stage, accounting judgements can be difficult because of the high degree of uncertainty associated with determining whether a present obligation exists, and estimating the probability and amount of any outflows that may arise. As matters progress, management and legal advisers evaluate on an ongoing basis whether provisions should be recognised, revising previous estimates as appropriate. At more advanced stages, it is typically easier to make estimates around a better defined set of possible outcomes.	• Provisions for legal proceedings and regulatory matters remain very sensitive to the assumptions used in the estimate. There could be a wider range of possible outcomes for any pending legal proceedings, investigations or inquiries. As a result it is often not practicable to quantify a range of possible outcomes for individual matters. It is also not practicable to meaningfully quantify ranges of potential outcomes in aggregate for these types of provisions because of the diverse nature and circumstances of such matters and the wide range of uncertainties involved. • Provisions for customer remediation also require significant levels of estimation. The amounts of provisions recognised depend on a number of different assumptions, such as the volume of inbound complaints, the projected period of inbound complaint volumes, the decay rate of complaint volumes, the populations identified as systemically mis-sold and the number of policies per customer complaint. More information about these assumptions is included in Note 19.

Contingent liabilities, contractual commitments and guarantees

Contingent liabilities

Contingent liabilities, which include certain guarantees and letters of credit pledged as collateral security, and contingent liabilities related to legal proceedings or regulatory matters, are not recognised in the financial statements but are disclosed unless the probability of settlement is remote.

Financial guarantee contracts

Liabilities under financial guarantee contracts that are not classified as insurance contracts are recorded initially at their fair value, which is generally the fee received or present value of the fee receivable.

2 Net fee income

	Year ended	
	31 Dec 2019	31 Dec 2018
Net fee income by product	**£m**	£m
Account services	**583**	362
Funds under management	**88**	46
Cards	**281**	145
Credit facilities	**103**	72
Imports/exports	**49**	21
Insurance agency commission	**47**	27
Receivables finance	**85**	37
Other	**220**	121
Fee income	**1,456**	831
Less: fee expense	**(226)**	(183)
Net fee income	**1,230**	648
Net fee income by global business		
Retail Banking and Wealth Management	**660**	341
Commercial Banking	**725**	378
Global Banking and Markets	**(180)**	(98)
Private Banking	**35**	12
Corporate Centre	**(10)**	15

Net fee income includes £1,125m of fees earned on financial assets that are not at fair value through profit or loss (other than amounts included in determining the effective interest rate) (2018: £636m), £174m of fees payable on financial liabilities that are not at fair value through profit of loss (other than amounts included in determining the effective interest rate) (2018: £117m), £69m of fees earned on trust and other fiduciary activities (2018: £50m) and Nil fees payable relating to trust and other fiduciary activities (2018: £2m).

3 Employee compensation and benefits

	2019	2018
	£m	£m
Wages and salaries	**887**	400
Social security costs	**89**	44
Post-employment benefits[1]	**(42)**	167
Year ended 31 Dec	**934**	611

1 *Includes a £187m past service cost in respect of GMP equalisation in 2018.*

Average number of persons employed by the group during the year

	2019	2018 [1]
Retail Banking and Wealth Management	**17,356**	8,739
Commercial Banking	**5,058**	2,424
Global Banking and Markets	**54**	26
Private Banking	**294**	137
Corporate Centre	**273**	151
Year ended 31 Dec	**23,035**	11,477

1 *In October 2017, 21,571 employees were transferred from HSBC Bank plc to the group, and were seconded back to HSBC Bank plc until 30 June 2018. Numbers exclude staff seconded to HSBC Bank plc until 30 June 2018.*

Share-based payments

The share-based payment income statement charge is recognised in wages and salaries as follows:

	2019 £m	2018 £m
Restricted share awards	**6**	—
Savings-related and other share award option plans	**10**	7
Year ended 31 Dec	**16**	7

HSBC Group share awards

Award	Policy
Deferred share awards (including annual incentive awards, LTI awards delivered in shares) and GPSP	• An assessment of performance over the relevant period ending on 31 December is used to determine the amount of the award to be granted. • Deferred awards generally require employees to remain in employment over the vesting period and are not subject to performance conditions after the grant date. • Deferred share awards generally vest over a period of three, five or seven years. • Vested shares may be subject to a retention requirement post-vesting. GPSP awards are retained until cessation of employment. • Awards granted from 2010 onwards are subject to a malus provision prior to vesting. • Awards granted to Market Risk Takers from 2015 onwards are subject to clawback post vesting.
International Employee Share Purchase Plan ('ShareMatch')	• The plan was first introduced in Hong Kong in 2013 and now includes employees based in 27 jurisdictions. • Shares are purchased in the market each quarter up to a maximum value of £750, or the equivalent in local currency. • Matching awards are added at a ratio of one free share for every three purchased. • Matching awards vest subject to continued employment and the retention of the purchased shares for a maximum period of two years and nine months.

Movement on HSBC share awards

	2019 Number (000s)	2018 Number (000s)
Restricted share awards outstanding at 1 Jan	**999**	—
Transfer from HSBC Bank plc and other Group subsidiaries	**N/A**	1,126
Additions during the year	**1,156**	20
Released in the year	**(831)**	(143)
Forfeited in the year	**(36)**	(4)
Restricted share awards outstanding at 31 Dec	**1,288**	999
Weighted average fair value of awards granted (£)	**5.98**	1.33

HSBC Group share option plans

Plans	Policy
Savings-related share option plans ('Sharesave')	• Eligible employees can save up to £500 per month with the option to use the savings to acquire shares. • Exercisable within six months following either the third or fifth anniversary of the commencement of a three-year or five-year contract, respectively. • The exercise price is set at a 20% (2018: 20%) discount to the market value immediately preceding the date of invitation.

Calculation of fair values

The fair values of share options are calculated using a Black-Scholes model. The fair value of a share award is based on the share price at the date of the grant.

Movement on HSBC Group share option plans

	Savings-related	
	Number (000s)	WAEP[1] £
Outstanding at 1 Jan 2019	**24,463**	**4.97**
Granted during the year	**14,125**	**4.69**
Exercised during the year	**(5,152)**	**4.43**
Expired during the year	**(37)**	**4.24**
Forfeited during the year	**(4,929)**	**5.45**
Outstanding at 31 Dec 2019	**28,470**	**4.84**
Of which exercisable	**891**	**4.53**
Weighted average remaining contractual life (years)	**2.78**	
Outstanding at 1 Jan 2018	—	0.00
Transfer from HSBC Bank plc and other Group subsidiaries	27,064	4.51
Granted during the year	8,803	5.45
Exercised during the year	(10,294)	4.15
Expired during the year	(879)	5.37
Forfeited during the year	(231)	4.70
Outstanding at 31 Dec 2018	24,463	4.97
Of which exercisable	1,218	4.10
Weighted average remaining contractual life (years)	2.59	

1 *Weighted average exercise price.*

Post-employment benefit plans

We operate a pension plan for our employees called the HSBC Bank (UK) Pension Scheme ('the plan'), which has both defined benefit and defined contribution sections. To meet the requirements of the Banking Reform Act, from 1 July 2018, the main employer of the plan changed from HSBC Bank plc to HSBC UK Bank plc, with additional support from HSBC Holdings plc. At that time, the non-ring fenced entities including HSBC Bank plc exited the section of the plan for ring-fenced entities (the 'HSBC UK section') and joined a newly created section for the future defined benefit and defined contribution pension benefits of their employees.

The Pension Risk section on page 46 contains details about the policies and practices associated with the plan.

The defined benefit section was closed to future benefit accrual in 2015, with Group defined benefits earned by employees at that date continuing to be linked to their salary while they remain employed by HSBC. The plan is overseen by an independent corporate trustee, who has a fiduciary responsibility for the operation of the plan. Its assets are held separately from the assets of the group.

The investment strategy of the plan is to hold the majority of assets in bonds, with the remainder in a diverse range of investments. It also includes some interest rate swaps to reduce interest rate risk and inflation swaps to reduce inflation risk.

The latest funding valuation of the plan at 31 December 2016 was carried out by Colin G Singer, at Willis Towers Watson Limited, who is a Fellow of the UK Institute and Faculty of Actuaries, using the projected unit credit method. At that date, the market value of the plan's assets was £28.8bn and this exceeded the value placed on its liabilities on an ongoing basis by £1.4bn, giving a funding level of 105%. These figures relate only to the HSBC UK section of the plan and include defined contribution assets amounting to £2.0bn. The main differences between the assumptions used for assessing the liabilities for this funding valuation and those used for IAS 19 are more prudent assumptions for discount rate, inflation rate and life expectancy. The next funding valuation will have an effective date of 31 December 2019.

Although the plan was in surplus at the valuation date, further contributions will be made to the plan to support a lower-risk investment strategy over the longer term. The remaining contributions are £160m in each of 2020 and 2021.

The actuary also assessed the value of the liabilities the HSBC UK section of the plan were to be stopped and an insurance company asked to secure all future pension payments. This is generally larger than the amount needed on the ongoing basis described above because an insurance company would use more prudent assumptions and include an explicit allowance for the future administrative expenses of the plan. Under this approach, the amount of assets needed was estimated to be £37bn at 31 December 2016.

The Trust Deed gives the ability for HSBC UK to take a refund of surplus assets after the plan has been run down such that no further beneficiaries remain. On this basis, any net surplus in the HSBC UK section of the plan is recognised in the group's financial statements.

Guaranteed Minimum Pension Equalisation

Following a judgement issued by the High Court of Justice of England and Wales in 2018, we estimated the financial effect of equalising benefits in respect of guaranteed minimum pensions ('GMP') equalisation, and any potential conversion of GMPs into non-GMP benefits, to be an approximate 0.9% increase in the plan's liabilities, or £187m. This was recognised in the Income Statement in 2018. We continue to assess the impact of GMP equalisation, however no further amounts have been recognised in 2019.

Income statement charge

	2019 £m	2018 £m
Defined benefit pension plans[1]	**(115)**	122
Defined contribution pension plans	**73**	44
Pension plans	**(42)**	166
Year ended 31 Dec	**(42)**	166

1 *Includes a £187m past service cost in respect of GMP equalisation in 2018.*

Defined benefit pension plans

Net asset/(liability) under defined benefit pension plans

	Fair value of plan assets	Present value of defined benefit obligations	Net defined benefit assets/(liabilities)
	£m	£m	£m
At 1 Jan 2019	**26,687**	**(20,846)**	**5,841**
Service cost	**–**	**(26)**	**(26)**
Current service cost	**–**	**(7)**	**(7)**
Past service cost and gains/(losses) from settlements	**–**	**(19)**	**(19)**
Net interest income/(cost) on the net defined benefit asset/(liability)	**736**	**(571)**	**165**
Remeasurement effects recognised in other comprehensive income	**1,729**	**(1,998)**	**(269)**
– return on plan assets (excluding interest income)	**1,729**	**–**	**1,729**
– actuarial losses	**–**	**(2,392)**	**(2,392)**
– other changes		**394**	**394**
Exchange differences	**195**	**(162)**	**33**
Benefits paid	**(795)**	**795**	**–**
Other movements[1]	**95**	**(3)**	**92**
At 31 Dec 2019	**28,647**	**(22,811)**	**5,836**
At 1 Jan 2018	–	–	–
Transfer in from HSBC Bank plc on 1 July 2018	26,948	(20,580)	6,368
Service cost	–	(189)	(189)
Current service cost	–	(2)	(2)
Past service cost and gains/(losses) from settlements	–	(187)	(187)
Net interest income/(cost) on the net defined benefit asset/(liability)	358	(279)	79
Remeasurement effects recognised in other comprehensive income	(279)	(206)	(485)
– return on plan assets (excluding interest income)	(279)	–	(279)
– actuarial losses	–	(186)	(186)
– other changes	–	(20)	(20)
Exchange differences	–	–	–
Benefits paid	(405)	405	–
Other movements[1]	65	3	68
At 31 Dec 2018	26,687	(20,846)	5,841

1 Other movements include contributions by HSBC UK, contributions by employees, administrative costs and taxes paid by plan.

HSBC UK expects to make £160m of contributions to defined benefit pension plans during 2020. Benefits expected to be paid from the HSBC UK Pension Scheme to retirees over each of the next five years, and in aggregate for the five years thereafter, are as follows:

Benefits expected to be paid from plan

	2020	2021	2022	2023	2024	2025–2029
	£m	£m	£m	£m	£m	£m
The plan[1]	818	842	866	891	917	5,000

1 The duration of the defined benefit obligation is 18.1 years under the disclosure assumptions adopted (2018:17.0 years).

Fair value of plan assets by asset classes

	31 Dec 2019			31 Dec 2018		
	Value	Quoted market price in active market	No quoted market price in active market	Value	Quoted market price in active market	No quoted market price in active market
	£m	£m	£m	£m	£m	£m
The plan						
Fair value of plan assets	**28,647**	**25,658**	**2,989**	26,687	23,710	2,977
– equities	**501**	**236**	**265**	2,468	2,101	367
– bonds	**23,976**	**23,976**	**–**	20,763	20,763	–
– derivatives	**1,551**	**–**	**1,551**	1,618	–	1,618
– other	**2,619**	**1,446**	**1,173**	1,838	846	992

Post-employment defined benefit plan actuarial financial assumptions

The group determines the discount rates to be applied to its obligations in consultation with the plans' local actuaries, on the basis of current average yields of high quality (AA-rated or equivalent) debt instruments with maturities consistent with those of the defined benefit obligations.

Key actuarial assumptions for the plan

	Discount rate	Inflation rate	Rate of increase for pensions	Rate of pay increase
	%	%	%	%
UK				
At 31 Dec 2019	**2.00**	**3.10**	**2.90**	**3.65**
At 31 Dec 2018	2.80	3.40	3.10	3.65

Mortality tables and average life expectancy at age 60 for the plan

UK	Mortality table	Life expectancy at age 60[3] for a male member currently:		Life expectancy at age 60[3] for a female member currently:	
		Aged 60	Aged 40	Aged 60	Aged 40
At 31 Dec 2019	**SAPS S2[1]**	**28.0**	**29.4**	**28.2**	**29.8**
At 31 Dec 2018	SAPS S2[2]	28.1	29.6	28.4	30.0

1 *Self-administered pension scheme ('SAPS') S2 table (males: 'Normal Health Pensioners' version; females: 'All Pensioners' version) with a multiplier of 0.94 for males and 1.15 for females. Improvements are projected in accordance with the Continuous Mortality Investigation ('CMI') 2018 core projection model with an initial addition to improvements of 0.25% per annum and a long-term rate of improvement of 1.25% per annum. Separate tables have been applied to lower paid pensioners and dependant members.*
2 *Self-administered pension scheme ('SAPS') S2 table (males: 'Normal Health Pensioners' version; females: 'All Pensioners' version) with a multiplier of 0.94 for males and 1.15 for females. Improvements are projected in accordance with the Continuous Mortality Investigation ('CMI') 2017 core projection model with a long-term rate of improvement of 1.25% per annum. Separate tables have been applied to lower paid pensioners and dependant members.*
3 *The presentation of the mortality table has been updated to show life expectancies at the age of 60 rather than 65 as presented in prior years to better reflect market disclosure practices. The prior year data has been updated accordingly.*

The effect of changes in key assumptions on the plan

	Impact on HSBC Bank (UK) Pension Scheme Obligation			
	Financial impact of increase		Financial impact of decrease	
	2019 £m	2018 £m	**2019 £m**	2018 £m
Discount rate – increase/decrease of 0.25%	**(987)**	(844)[1]	**1,055**	900
Inflation rate – increase/decrease of 0.25%	**590**	569	**(559)**	(562)
Pension payments and deferred pensions – increase/decrease of 0.25%	**639**	926	**(776)**	(870)
Pay – increase/decrease of 0.25%	**54**	22	**(55)**	(23)
Change in mortality – increase of 1 year	**958**	771	**N/A**	N/A

Directors' emoluments

The aggregate emoluments of the Directors of the bank, computed in accordance with the Companies Act 2006 as amended by statutory instrument 2008 No.410, were:

	2019 £000	2018 £000
Fees paid to non-executive Directors	**1,793**	1,262
Salaries and other emoluments[1,2]	**3,459**	1,366
Annual incentives[2,3]	**901**	495
Long-term incentives[2,4]	**253**	295
Year ended 31 Dec	**6,406**	3,418

1 *Salaries and other emoluments include Fixed Pay Allowances.*
2 *During the first six months of 2018 the banks' Executive Directors provided services to other companies within the HSBC Group and their services to the bank were incidental. Therefore the Executive Directors remuneration for 2018 disclosed represents the period from 1 July to 31 December 2018.*
3 *Discretionary annual incentives for the Executive Directors are based on a combination of individual and corporate performance and are determined by the Remuneration Committee of the bank's ultimate parent company, HSBC Holdings plc. Incentive awards made to Executive Directors are delivered in the form of cash and HSBC Holdings plc shares. The total amount shown is comprised of £450,576 (2018: £247,275) in cash and £450,576 (2018: £247,275) in Restricted Shares, which is the upfront portion of the annual incentive granted in respect of performance year 2019.*
4 *The amount shown is comprised of £125,505 (2018: £120,000) in deferred cash and £127,395 (2018: £175,358) in deferred Restricted Shares. These amounts relate to the portion of the awards that will vest following the substantial completion of the vesting condition attached to these awards in 2019. The total deferral period of deferred cash and share awards is no less than 5 years up to a maximum of 7 years. Grants with a 5 year deferral vest in 5 equal tranches on each anniversary of the grant date on a pro-rate basis. Grants with a 7 year deferral vest in 5 equal tranches on each anniversary from the 3rd anniversary of the grant date on a pro-rata basis.. The deferral periods and pro-rata calculations are in line with the requirements set out in the Remuneration rules applicable to Material Risk Takers. The share awards are subject to a retention period of 6 months to 1 year upon vesting. Details of the Plans are contained within the Directors' Remuneration Report of HSBC Holdings plc.*

No Directors exercised share options over HSBC Holdings plc ordinary shares during the year (2018: 1).

Awards were made to three Directors under long-term incentive plans in respect of qualifying services rendered in 2019 (2018: 3). During 2019, three Directors received shares in respect of awards under long-term incentive plans that vested during the year (2018: 3).

No retirement benefits accrued to Directors during the year in respect of their qualifying services (2018: no Directors). Three Directors received cash in lieu of pension contributions during the year in respect of their qualifying services. Cash received in lieu of pension is included in the salary and other emoluments disclosure in the table above.

Of these aggregate figures, the following amounts are attributable to the highest paid Director:

	2019 £000	2018 £000
Salaries and other emoluments[3]	**2,104**	776
Annual incentives[1,3]	**503**	274
Long-term incentives[2,3]	**124**	176
Year ended 31 Dec	**2,731**	1,226

1 *Awards made to the highest paid Director are delivered in the form of cash and HSBC Holdings plc shares. The amount shown is comprised of £251,721 (2018: £136,805) in cash and £251,721(2018: £136,805) in Restricted Shares.*
2 *The amount shown is comprised of £60,472 (2018: £66,575) in deferred cash and £63,902 (2018: £109,145) in deferred Restricted Shares. These amounts relate to a portion of the awards that will vest following the substantial completion of the vesting condition attached to these awards in 2019. The total deferral period of deferred cash and share awards is 7 years with the deferred awards subject to pro-rata vesting in five equal tranches between the third and seventh anniversary of grant. The share awards are subject to a one year retention period upon vesting.*
3 *During the first six months of 2018 the bank's Executive Directors provided services to other companies within the HSBC Group and their services to the bank were incidental. Therefore the Executive Directors remuneration disclosed represents the period from 1 July to 31 December 2018.*

The highest paid Director received shares in respect of qualifying services under a long-term incentive scheme.

Pension contributions of £nil were made by the bank in respect of services by the highest paid Director during the year (2018: £nil).

4 Auditors' remuneration

	2019 £m	2018 £m
Audit fees payable to PwC	**5.1**	4.3
Other audit fees payable	**1.8**	0.7
Year ended 31 Dec	**6.9**	5.0

Fees payable by the group to PwC

	2019 £m	2018 £m
Audit fees for HSBC UK Bank plc's statutory audit[1]	**4.0**	3.6
Fees for other services provided to the group	**2.9**	1.4
– audit of the group's subsidiaries[2]	**1.1**	0.7
– audit-related assurance services[3]	**1.8**	0.7
Year ended 31 Dec	**6.9**	5.0

1 *Fees payable to PwC for the statutory audit of the consolidated financial statements of the group and the separate financial statements of HSBC UK Bank plc. They exclude amounts payable for the statutory audit of the bank's subsidiaries which have been included in 'Fees for other services provided to the group'.*
2 *Including fees payable to PwC for the statutory audit of the bank's subsidiaries.*
3 *Including services for assurance and other services that relate to statutory and regulatory filings, including comfort letters and interim and quarter reviews.*

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

Fees payable for non-audit services for HSBC UK Bank plc are not disclosed separately because such fees are disclosed on a consolidated basis for the group.

5 Tax

Tax expense

	2019 £m	2018 £m
Current tax	**429**	321
– for this year	**452**	323
– adjustments in respect of prior years	**(23)**	(2)
Deferred tax	**65**	(20)
– origination and reversal of temporary differences	**71**	(21)
– effect of changes in tax rates	**(4)**	2
– adjustments in respect of prior years	**(2)**	(1)
Year ended 31 Dec	**494**	301

The tax rate applying to HSBC UK Bank plc and its banking subsidiaries was 27%, comprising 19% UK corporation tax rate plus 8% surcharge tax rate on UK banking profits. The tax rate applicable for non-banking entities is 19% (2018: 19%).

Tax reconciliation

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

	2019 £m	2019 %	2018 £m	2018 %
Profit before tax	**1,010**		1,064	
Tax expense				
Taxation at UK corporation tax of 19.00% (2018: 19.00%)	**192**	**19.0**	202	19.0
Items increasing the tax charge in 2019:				
– non-deductible UK customer redress	**301**	**29.8**	15	1.3
– UK banking surcharge	**73**	**7.2**	80	7.6
Items reducing tax charge in 2019:				
– deductions for AT1 coupon payments	**(36)**	**(3.6)**	–	–
– adjustments in respect of prior period liabilities	**(25)**	**(2.4)**	(3)	(0.2)
– other permanent disallowables	**(7)**	**(0.7)**	5	0.5
– change in tax rates	**(4)**	**(0.4)**	2	0.1
Year ended 31 Dec	**494**	**48.9**	301	28.3

The effective tax rate for the year was 48.9% (2018: 28.3%), reflecting the UK rate of corporation tax for banking entities of 27% (2018: 27%), the tax impact of non-deductible redress provisions of £301m (2018: £15m) offset by the tax impact of deductions for additional tier 1 coupon payments of £36m recognised in the income statement tax charge, following a change to IAS 12 effective from 1 January 2019. 2018 was not restated for this change.

Redress provisions associated with PPI and certain other customer redress are not deductible for tax in the UK and, additionally, give rise to an increase in taxable profit equal to 10% of the redress incurred.

Movement of deferred tax assets and liabilities

	Loan impairment provisions £m	Cash flow hedges £m	FVOCI reserves £m	Defined benefit pension £m	Fixed and intangible assets £m	Other £m	Total £m
The group							
At 1 Jan 2019	**147**	**16**	**(4)**	**(1,460)**	**99**	**13**	**(1,189)**
Income statement	**(17)**	**–**	**–**	**(41)**	**(1)**	**(6)**	**(65)**
Other comprehensive income	**–**	**(12)**	**1**	**42**	**–**		**31**
At 31 Dec 2019	**130**	**4**	**(3)**	**(1,459)**	**98**	**7**	**(1,223)**
Assets	**130**	**4**			**98**	**7**	**239**
Liabilities	**–**	**–**	**(3)**	**(1,459)**	**–**	**–**	**(1,462)**
At 1 Jan 2018	–	–	–	–	–	–	–
Transfer from HSBC Bank plc and its subsidiaries	156	10	(1)	(1,592)	87	6	(1,334)
Income statement	(9)	–	–	11	12	7	21
Other comprehensive income	–	6	(3)	121	–	–	124
At 31 Dec 2018	147	16	(4)	(1,460)	99	13	(1,189)
Assets	147	16	–	–	99	13	275
Liabilities	–	–	(4)	(1,460)	–	–	(1,464)

Movement of deferred tax assets and liabilities

	Loan impairment provisions £m	Cash flow hedges £m	FVOCI reserves £m	Defined benefit pension £m	Fixed and intangible assets £m	Other £m	Total £m
The bank							
At 1 Jan 2019	**137**	**16**	**(4)**	**(1,460)**	**81**	**6**	**(1,224)**
Income statement	**(16)**	**–**	**–**	**(41)**	**(1)**	**(4)**	**(62)**
Other comprehensive income	**–**	**(12)**	**1**	**42**	**–**	**–**	**31**
At 31 Dec 2019	**121**	**4**	**(3)**	**(1,459)**	**80**	**2**	**(1,255)**
Assets	**121**	**4**	**–**	**–**	**80**	**2**	**207**
Liabilities	**–**	**–**	**(3)**	**(1,459)**	**–**	**–**	**(1,462)**
At 1 Jan 2018	–	–	–	–	–	–	–
Transfer from HSBC Bank plc	145	10	(1)	(1,592)	70	–	(1,368)
Income statement	(8)	–	–	11	11	6	20
Other comprehensive income	–	6	(3)	121	–	–	124
At 31 Dec 2018	137	16	(4)	(1,460)	81	6	(1,224)
Assets	137	16	–	–	81	6	240
Liabilities	–	–	(4)	(1,460)	–	–	(1,464)

Based on the enacted law at 31 December 2019, the UK corporation tax rate is due to reduce from 19% to 17% on 1 April 2020. The Conservative Party (now in Government) has indicated its intention to reverse this rate reduction as part of the UK Budget on 11 March 2020, which, if enacted, will result in a £98m increase to the group's (£100m increase to the bank's) net deferred tax liability, as at 31 December 2019.

6 Dividends

Dividends to the shareholder of the parent company

	2019		2018	
	£ per share	£m	£ per share	£m
Dividends paid on ordinary shares				
Interim dividend in respect of the previous year	**4,000**	**200**	–	–
Interim dividend in respect of the current year	**2,400**	**120**	–	–
Total	**6,400**	**320**	–	–

On 13 February 2020, the Directors declared an interim dividend to the ordinary shareholder of £100m in respect of the financial year ending 31 December 2019 which will be payable on 19 March 2020. No liability is recognised in the financial statements in respect of this dividend.

Total coupons on capital securities classified as equity

	First call date	2019 £m	2018 £m
Undated Subordinated Additional Tier 1 instruments			
– £1,096m	Dec 2019	**65**	–
– £1,100m	Dec 2024	**66**	–
Total		**131**	–

7 Fair values of financial instruments carried at fair value

Control framework

Fair values are subject to a control framework designed to ensure that they are either determined or validated by a function independent of the risk taker.

Where fair values are determined by reference to externally quoted prices or observable pricing inputs to models, independent price determination or validation is used.

For fair values determined using valuation models, the control framework includes development or validation by independent support functions of the model logic, inputs, model outputs and adjustments. Valuation models are subject to a process of due diligence before becoming operational and are calibrated against external market data on an ongoing basis.

Changes in fair value are generally subject to a profit and loss analysis process and are disaggregated into high-level categories including portfolio changes, market movements and other fair value adjustments.

Fair value hierarchy

Fair values of financial assets and liabilities are determined according to the following hierarchy:

- Level 1 – valuation technique using quoted market price: financial instruments with quoted prices for identical instruments in active markets that can be accessed at the measurement date.
- Level 2 – valuation technique using observable inputs: financial instruments with quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in inactive markets and financial instruments valued using models where all significant inputs are observable.
- Level 3 – valuation technique with significant unobservable inputs: financial instruments valued using valuation techniques where one or more significant inputs are unobservable.

Financial instruments carried at fair value and bases of valuation

	2019				2018			
The group	**Level 1 £m**	**Level 2 £m**	**Level 3 £m**	**Total £m**	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Recurring fair value measurements at 31 Dec								
Assets								
Financial assets designated and otherwise mandatorily measured at fair value through profit or loss	**65**	**1**	–	**66**	34	1	–	35
Derivatives	**2**	**119**	–	**121**	2	64	–	66
Financial investments	**19,285**	**452**	–	**19,737**	12,613	590	–	13,203
Liabilities								
Derivatives	**4**	**197**	–	**201**	1	345	–	346
The bank								
Recurring fair value measurements at 31 Dec								
Assets								
Financial assets designated and otherwise mandatorily measured at fair value through profit or loss	**65**	**1**	–	**66**	34	1	–	35
Derivatives	**2**	**116**	–	**118**	2	59	–	61
Financial investments	**19,285**	**452**	–	**19,737**	12,613	590	–	13,203
Liabilities								
Derivatives	**3**	**194**	–	**197**	1	340	–	341

Transfers between levels of the fair value hierarchy are deemed to occur at the end of each quarterly reporting period. Transfers into and out of levels of the fair value hierarchy are primarily attributable to observability of valuation inputs and price transparency. There were no transfers between Level 1 and Level 2 during 2019 and 2018.

Fair value adjustments

Fair value adjustments are adopted when the group determines there are additional factors considered by market participants that are not incorporated within the valuation model. Movements in the level of fair value adjustments do not necessarily result in the recognition of profits or losses within the income statement, such as when models are enhanced and therefore fair value adjustments may no longer be required.

8 Fair values of financial instruments not carried at fair value

Fair values of financial instruments not carried at fair value and bases of valuation

		Fair value			
	Carrying amount	Quoted market price Level 1	Observable inputs Level 2	Significant unobservable inputs Level 3	Total
	£m	£m	£m	£m	£m
The group					
At 31 Dec 2019					
Assets					
Loans and advances to banks	**1,389**	**–**	**1,389**	**–**	**1,389**
Loans and advances to customers	**183,056**	**–**	**531**	**183,744**	**184,275**
Reverse repurchase agreements – non-trading	**3,014**	**–**	**3,014**	**–**	**3,014**
Liabilities					
Deposits by banks	**529**	**–**	**529**	**–**	**529**
Customer accounts	**216,214**	**–**	**216,214**	**–**	**216,214**
Repurchase agreements – non-trading	**98**	**–**	**98**	**–**	**98**
Debt securities in issue	**3,142**	**–**	**3,142**	**–**	**3,142**
Subordinated liabilities	**9,533**	**–**	**10,094**	**–**	**10,094**
At 31 Dec 2018					
Assets					
Loans and advances to banks	1,263	–	1,263	–	1,263
Loans and advances to customers	174,807	–	631	176,229	176,860
Reverse repurchase agreements – non-trading	3,422	–	3,422	–	3,422
Liabilities					
Deposits by banks	1,027	–	1,027	–	1,027
Customer accounts	204,837	–	204,818	–	204,818
Repurchase agreements – non-trading	639	–	639	–	639
Debt securities in issue	–	–	–	–	–
Subordinated liabilities	4,937	–	5,040	–	5,040
The bank					
At 31 Dec 2019					
Assets					
Loans and advances to banks	**4,643**	**–**	**4,643**	**–**	**4,643**
Loans and advances to customers	**173,901**	**–**	**531**	**174,480**	**175,011**
Reverse repurchase agreements – non-trading	**3,014**	**–**	**3,014**	**–**	**3,014**
Liabilities					
Deposits by banks	**4,277**	**–**	**4,277**	**–**	**4,277**
Customer accounts	**207,830**	**–**	**207,830**	**–**	**207,830**
Repurchase agreements – non-trading	**98**	**–**	**98**	**–**	**98**
Debt securities in issue	**2,917**	**–**	**2,917**	**–**	**2,917**
Subordinated liabilities	**9,454**	**–**	**10,015**	**–**	**10,015**
At 31 Dec 2018					
Assets					
Loans and advances to banks	3,883	–	3,883	–	3,883
Loans and advances to customers	165,850	–	631	167,468	168,099
Reverse repurchase agreements – non-trading	3,422	–	3,422	–	3,422
Liabilities					
Deposits by banks	4,265	–	4,265	–	4,265
Customer accounts	196,858	–	196,858	–	196,858
Repurchase agreements – non-trading	639	–	639	–	639
Debt securities in issue	–	–	–	–	–
Subordinated liabilities	4,858	–	4,961	–	4,961

Other financial instruments not carried at fair value are typically short-term in nature and reprice to current market rates frequently. Accordingly, their carrying amount is a reasonable approximation of fair value. They include cash and balances at central banks and items in the course of collection from and transmission to other banks, all of which are measured at amortised cost.

Valuation

Fair value is an estimate of the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. It does not reflect the economic benefits and costs that the group expects to flow from an instrument's cash flow over its expected future life. Our valuation methodologies and assumptions in determining fair values for which no observable market prices are available may differ from those of other companies.

Loans and advances to banks and customers

To determine the fair value of loans and advances to banks and customers, loans are segregated into portfolios of similar characteristics. Where applicable fair value is measured using quoted price for similar assets in and active market, where not applicable the fair value of the portfolios is determined using internal pricing models using external market data, and discounting future cash flows to present value.

The fair value of loans reflects expected credit losses at the balance sheet date and estimates of market participants' expectations of credit losses over the life of the loans, and the fair value effect of repricing between origination and the balance sheet date. For credit impaired loans, fair value is estimated by discounting the future cash flows over the time period they are expected to be recovered.

Deposits by banks and customer accounts

The fair values of on-demand deposits are approximated by their carrying value. For deposits with longer-term maturities, fair values are estimated using discounted cash flows, applying current rates offered for deposits of similar remaining maturities.

Debt securities in issue and subordinated liabilities

Fair values are determined using quoted market prices at the balance sheet date where available, or by reference to quoted market prices for similar instruments.

Repurchase and reverse repurchase agreements – non-trading

Fair values approximate carrying amounts as balances are generally short dated.

9 Derivatives

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

	Notional contract amount		*Fair value – Assets*			*Fair value – Liabilities*		
	Trading	Hedging	Trading	Hedging	Total	Trading	Hedging	Total
The group	£m	£m	£m	£m	£m	£m	£m	£m
Foreign exchange	**7,733**	**803**	**64**	**2**	**66**	**65**	**14**	**79**
Interest rate	**9,405**	**20,250**	**340**	**288**	**628**	**342**	**353**	**695**
Gross total fair values	**17,138**	**21,053**	**404**	**290**	**694**	**407**	**367**	**774**
Offset (Note 22)					**(573)**			**(573)**
At 31 Dec 2019	**17,138**	**21,053**	**404**	**290**	**121**	**407**	**367**	**201**
Foreign exchange	5,740	2,222	42	5	47	44	79	123
Interest rate	15,587	12,522	142	79	221	133	292	425
Gross total fair values	21,327	14,744	184	84	268	177	371	548
Offset (Note 22)					(202)			(202)
At 31 Dec 2018	21,327	14,744	184	84	66	177	371	346

	Notional contract amount		Fair value – Assets			Fair value – Liabilities		
	Trading	Hedging	Trading	Hedging	Total	Trading	Hedging	Total
The bank	£m	£m	£m	£m	£m	£m	£m	£m
Foreign exchange	**7,355**	**803**	**60**	**2**	**62**	**61**	**14**	**75**
Interest rate	**9,385**	**20,251**	**341**	**288**	**629**	**342**	**353**	**695**
Gross total fair values	**16,740**	**21,054**	**401**	**290**	**691**	**403**	**367**	**770**
Offset (Note 22)					**(573)**			**(573)**
At 31 Dec 2019	**16,740**	**21,054**	**401**	**290**	**118**	**403**	**367**	**197**
Foreign exchange	5,189	2,222	37	5	42	38	79	117
Interest rate	15,567	12,522	142	79	221	133	293	426
Gross total fair values	20,756	14,744	179	84	263	171	372	543
Offset (Note 22)					(202)			(202)
At 31 Dec 2018	20,756	14,744	179	84	61	171	372	341

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

Use of derivatives

We undertake derivative activity for two primary purposes: to create risk management solutions for clients and to manage and hedge our own risks.

Trading derivatives

Most of the group's derivative transactions relate to sales and trading activities. Sales activities include marketing of derivative products to customers to enable them to take, transfer, modify or reduce current or expected risks. Trading activities principally includes risk management. Risk management activity is undertaken to manage the risks arising from client transactions, with the principal purpose of retaining client margin. Other derivatives classified as held for trading include non-qualifying hedging derivatives.

Hedge accounting derivatives

The group applies hedge accounting to manage interest rate risk and foreign exchange risk. The 'Report of the Directors Risk' presents more details on how these risks arise and how they are managed by the group.

Fair value hedges

The group enters into fixed-for-floating-interest-rate swaps to manage the exposure to changes in fair value due to movements in market interest rates on certain fixed rate financial instruments which are not measured at fair value through profit or loss.

Hedging instrument by hedged risk

	Hedging Instrument				
		Carrying amount			
Hedged risk	Notional amount[1] £m	Assets £m	Liabilities £m	Balance sheet presentation	Change in fair value[2] £m
Interest rate[3]	17,740	280	350	Derivatives	62
At 31 Dec 2019	**17,740**	**280**	**350**		**62**
Interest rate[3]	8,762	63	278	Derivatives	(38)
At 31 Dec 2018	8,762	63	278		(38)

1 *The notional contract amounts of derivatives designated in qualifying hedge accounting relationships indicate the nominal value of transactions outstanding at the balance sheet date; they do not represent amounts at risk.*
2 *Used in effectiveness testing; comprising the full fair value change of the hedging instrument not excluding any component.*
3 *The hedged risk 'interest rate' includes inflation risk.*

Hedged item by hedged risk

	Hedged item						Ineffectiveness	
	Carrying amount		Accumulated fair value hedge adjustments included in carrying amount[2]			Change in fair value[1]	Recognised in profit and loss	
Hedged risk	Assets £m	Liabilities £m	Assets £m	Liabilities £m	Balance sheet presentation	£m	£m	Profit and loss presentation
Interest rate[4]	12,289		133		Financial assets designated and otherwise mandatorily measured at fair value through other comprehensive income	148	4	Net income from financial instruments hold for trading or managed on a fair value basis
		6,292		219	Subordinated Liabilities[3]	(206)		
At 31 Dec 2019	**12,289**	**6,292**	**133**	**219**		**(58)**	**4**	
Interest rate[4]	7,161		166		Financial assets designated and otherwise mandatorily measured at fair value through other comprehensive income	57	(2)	Net income from financial instruments held for trading or managed on a fair value basis
		2,033		21	Subordinated Liabilities[3]	(21)		
At 31 Dec 2018	7,161	2,033	166	21		36	(2)	

1 *Used in effectiveness assessment; comprising amount attributable to the designated hedged risk that can be a risk component.*
2 *The accumulated amount of fair value adjustments remaining in the statement of financial position for hedged items that have ceased to be adjusted for hedging gains and losses were liabilities of £26m (2018: £1.3m) for FVOCI.*
3 *The notional amount of non-dynamic fair value hedges is equal to £6,019m (2018: £2,000m), of which the weighted-average maturity date is June 2028 and the weighted average swap rate is 1.78% (2018: 1.45%). These hedges are all internal to HSBC Group and composed by internal funding between Group and HSBC UK.*
4 *The hedged risk 'interest rate' includes inflation risk.*

The hedged item is either the benchmark interest rate risk portion within the fixed rate of the hedged item or the full fixed rate and it is hedged for changes in fair value due to changes in the benchmark interest rate risk.

Sources of hedge ineffectiveness may arise from basis risk including but not limited to the discount rates used for calculating the fair value of derivatives, hedges using instruments with a non-zero fair value and notional and timing differences between the hedged items and hedging instruments.

The disclosures for the group are materially the same as the disclosures for the bank.

Cash flow hedges

The group's cash flow hedging instruments consist principally of interest rate swaps and cross-currency swaps that are used to manage the variability in future interest cash flows of non-trading financial assets and liabilities, arising due to changes in market interest rates and foreign-currency basis.

The group applies macro cash flow hedging for interest-rate risk exposures on portfolios of replenishing current and forecasted issuances of non-trading assets and liabilities that bear interest at variable rates, including rolling such instruments. The amounts and timing of future cash flows, representing both principal and interest flows, are projected for each portfolio of financial assets and liabilities on the basis of their contractual terms and other relevant factors, including estimates of prepayments and defaults. The aggregate cash flows representing both principal balances and interest cash flows across all portfolios are used to determine the effectiveness and ineffectiveness. Macro cash flow hedges are considered to be dynamic hedges.

The group also hedges the variability in future cash-flows on foreign-denominated financial assets and liabilities arising due to changes in foreign exchange market rates with cross-currency swaps, these are considered dynamic hedges.

Hedging instrument by hedged risk

	Hedging Instrument				Hedged Item		Ineffectiveness	
		Carrying amount			Change in fair value[2]	Change in fair value[3]	Recognised in profit and loss	
Hedged risk	Notional amount[1] £m	Assets £m	Liabilities £m	Balance sheet presentation	£m	£m	£m	Profit and loss presentation
Foreign currency	**803**	**2**	**14**	**Derivatives**	**16**	**16**	**–**	**Net income from financial instruments held for trading or managed on a fair value basis**
Interest rate	**2,510**	**8**	**3**	**Derivatives**	**24**	**23**	**1**	
At 31 Dec 2019	**3,313**	**10**	**17**		**40**	**39**	**1**	
Foreign currency	2,222	5	79	Derivatives	(110)	(110)	–	Net income from financial instruments held for trading or managed on a fair value basis
Interest rate	3,760	16	14	Derivatives	2	3	(1)	
At 31 Dec 2018	5,982	21	93		(108)	(107)	(1)	

1 *The notional contract amounts of derivatives designated in qualifying hedge accounting relationships indicate the nominal value of transactions outstanding at the balance sheet date; they do not represent amounts at risk.*
2 *Used in effectiveness testing; comprising the full fair value change of the hedging instrument not excluding any component.*
3 *Used in effectiveness assessment; comprising amount attributable to the designated hedged risk that can be a risk component.*

Sources of hedge ineffectiveness may arise from basis risk, including but not limited to timing differences between the hedged items and hedging instruments and hedges using instruments with a non-zero fair value.

During the year to 31 December 2019, a profit of £1m (2018: Loss of £1m) was recognised due to hedge ineffectiveness.

The disclosures for the group are materially the same as the disclosures for the bank.

Reconciliation of equity and analysis of other comprehensive income by risk type

	Interest rate £m	Foreign Currency £m
Cash flow hedging reserve at 1 Jan 2019	**(24)**	**(22)**
Fair value gains/(losses)	**23**	**16**
Fair value (gains)/losses reclassified from the cash flow hedge reserve to the income statement in respect of:		
– hedged items that have affected profit or loss	**(2)**	**9**
Income taxes	**(12)**	**–**
Cash flow hedging reserve at 31 Dec 2019	**(15)**	**3**
Cash flow hedging reserve at 1 Jan 2018	–	–
Fair value gains/(losses)	3	(110)
Fair value (gains)/losses reclassified from the cash flow hedge reserve to the income statement in respect of:		
– hedged items that have affected profit or loss	(7)	91
Income taxes	6	–
Transfer in from HSBC Bank plc	(26)	(3)
Cash flow hedging reserve at 31 Dec 2018	(24)	(22)

Interest Rate Benchmark Reform: Amendments to IFRS 9 and IAS 39 'Financial Instruments'

Following the request received by the Financial Stability Board from the G20, a fundamental review and reform of the major interest rate benchmarks is under way across the world's largest financial markets. This reform was not contemplated when the standard was published, and consequently the IASB has published a set of temporary exceptions from applying specific hedge accounting requirements to provide clarification on how the standard should be applied in these circumstances.

Amendments to IFRS 9 and IAS 39 were endorsed in January 2020 and modify specific hedge accounting requirements. Under these temporary exceptions, IBORs are assumed to continue for the purposes of hedge accounting until such time as the uncertainty is resolved.

The application of this set of temporary exceptions is mandatory for accounting periods starting on or after 1 January 2020, but early adoption is permitted and the group has elected to apply these exceptions for the year ended 31 December 2019. Significant judgement will be

required in determining when uncertainty is expected to be resolved and therefore when the temporary exceptions will cease to apply, however at 31 December 2019 the uncertainty exists and therefore the temporary exceptions apply to all of the group's hedge accounting relationships that reference Ibors.

The group has cash flow and fair value hedge accounting relationships that are exposed to different Ibors, predominantly US Dollar Libor, Sterling Libor, Eonia, and Euribor. Existing derivatives, loans, bonds, and other financial instruments designated in these relationships referencing Ibors will transition to new Risk-Free Rates ('RFRs') in different ways and at different times. External progress on the transition to RFRs is being monitored, with the objective of ensuring a smooth transition for the group's hedge accounting relationships. The specific issues arising will vary with the details of each hedging relationship, but may arise due to the transition of existing products included in the designation, a change in expected volumes of products to be issued, a change in contractual terms of new products issued, or a combination of these factors. Some hedges may need to be de-designated and new relationships entered into, while others may survive the transition.

The hedge accounting relationships that are affected by the adoption of the temporary exceptions hedge items presented in the Balance Sheet as 'Financial assets designated and otherwise mandatorily measured at fair value through other comprehensive income', 'Loans and advances to customers', 'Debt securities in issue', and 'Deposits by banks'.

The notional amounts of Interest Rate derivatives designated in hedge accounting relationships represent the extent of the risk exposure managed by the group that is directly affected by Ibor reform and impacted by the temporary exceptions. Although HSBC UK has designated hedge accounting relationships which involve cross currency swaps, these are not significant and have not been presented below:

Hedging instrument impacted by IBOR reform held by the group

	Hedging instrument					
	Impacted by IBOR reform				Not impacted by Ibor reform	Notional amount[1]
	€	£	$	Total		
	£m	£m	£m	£m	£m	£m
Fair value hedges	675	4,243	2,523	7,441	10,299	17,740
Cash flow hedges	–	2,210	–	2,210	300	2,510
At 31 Dec 2019	675	6,453	2,523	9,651	10,599	20,250

1 *The notional contract amounts of Interest Rate derivatives designated in qualifying hedge accounting relationships indicate the nominal value of transactions outstanding at the balance sheet date; they do not represent amounts at risk.*

For further risks and governance regarding the impact of the market-wide benchmarks reform, see Risk overview section on page 16.

10 Financial investments

Carrying amount of financial investments

	The group		The bank	
	2019	2018	2019	2018
	£m	£m	£m	£m
Financial investments measured at fair value through other comprehensive income	19,737	13,203	19,737	13,203
– treasury and other eligible bills	3,708	1,286	3,708	1,286
– debt securities	16,029	11,917	16,029	11,917
At 31 Dec	19,737	13,203	19,737	13,203

11 Assets pledged, collateral received and assets transferred

Assets pledged

Financial assets pledged as collateral

	The group		The bank	
	2019	2018	2019	2018
	£m	£m	£m	£m
Debt securities	3,238	4,324	3,238	4,324
Other	107	95	107	95
Assets pledged at 31 Dec	3,345	4,419	3,345	4,419

The amount of assets pledged to secure liabilities may be greater than the book value of assets utilised as collateral. For example, where assets are placed with a custodian or a settlement agent that has a floating charge over all the assets placed to secure any liabilities under settlement accounts.

These transactions are conducted under terms that are usual and customary to collateralised transactions including, where relevant, standard securities lending and borrowing, repurchase agreements and derivative margining. The group places both cash and non-cash collateral in relation to derivative transactions.

Financial assets pledged as collateral that the counterparty has the right to sell or repledge

	The group		The bank	
	2019	2018	2019	2018
	£m	£m	£m	£m
Financial investments	2,950	2,299	2,950	2,299
At 31 Dec	2,950	2,299	2,950	2,299

Collateral received

The fair value of assets accepted as collateral, relating primarily to standard securities lending, reverse repurchase agreements and derivative margining, that the group is permitted to sell or repledge in the absence of default was £3,691m (2018: £3,422m)
The bank: £3,691m (2018: £3,422m). The group is obliged to return equivalent securities. These transactions are conducted under terms that are usual and customary to standard securities lending, reverse repurchase agreements and derivative margining.

Assets transferred

The assets pledged include transfers to third parties that do not qualify for derecognition, notably secured borrowings such as debt securities held by counterparties as collateral under repurchase agreements and securities lent under securities lending agreements. For secured borrowings, the transferred asset collateral continues to be recognised in full and a related liability, reflecting the group's obligation to repurchase the assets for a fixed price at a future date is also recognised on the balance sheet. Where securities are swapped, the transferred asset continues to be recognised in full. There is no associated liability as the non-cash collateral received is not recognised on the balance sheet. The group is unable to use, sell or pledge the transferred assets for the duration of these transactions, and remains exposed to interest rate risk and credit risk on these pledged assets. The counterparty's recourse is not limited to the transferred assets.

Transferred financial assets not qualifying for full derecognition and associated financial liabilities

	2019		2018	
	Carrying amount of:		Carrying amount of:	
The group and bank	**Transferred assets £m**	**Associated liabilities £m**	Transferred assets £m	Associated liabilities £m
Repurchase agreements	**846**	**98**	727	639
Securities lending agreements	**2,104**	**–**	1,572	–

12 Interests in joint ventures

Interests in joint ventures

Vaultex UK Limited is a joint venture of the bank and the group. Vaultex UK Limited is incorporated in England and its principal activity is that of cash management services. At 31 December 2019, the group had a 50% interest in the £10m issued equity capital (2018: 50%).

For further detail see Note 29.

13 Investments in subsidiaries

Main subsidiaries of HSBC UK Bank plc

	Country of incorporation or registration	**HSBC UK Bank plc's interest in equity capital %**	**Share class**
HSBC Equipment Finance (UK) Limited	**England and Wales**	**100.00**	**Ordinary £1**
HSBC Invoice Finance (UK) Limited	**England and Wales**	**100.00**	**Ordinary £1**
HSBC Private Bank (UK) Limited	**England and Wales**	**100.00**	**Ordinary £10**
HSBC Trust Company (UK) Limited	**England and Wales**	**100.00**	**Ordinary £5**
Marks and Spencer Financial Services plc	**England and Wales**	**100.00**	**Ordinary £1**

All the above prepare their financial statements up to 31 December.

Details of all group subsidiaries, as required under Section 409 of the Companies Act 2006, are set out in Note 29. The principal country of operation is the same as the country of incorporation.

Impairment testing of investments in subsidiaries

At each reporting period end, HSBC UK Bank plc reviews investments in subsidiaries for indicators of impairment. An impairment is recognised when the carrying amount exceeds the recoverable amount for that investment.

The recoverable amount is the higher of the investment's fair value less costs of disposal and its value in use. The value in use is calculated by discounting management's cash flow projections for the investment.

- The cash flow projections for each investment are based on the latest approved plans and a long-term growth rate is used to extrapolate the cash flows in perpetuity.
- The growth rate reflects inflation and is based on the long-term average for the UK.
- The rate used to discount the cash flows is based on the cost of capital assigned to each investment, which is derived using a capital asset pricing model ('CAPM'). CAPM depends on a number of inputs reflecting financial and economic variables, including the risk-free rate and a premium to reflect the inherent risk of the business being evaluated. These variables are based on the market's assessment of the economic variables and management's judgement. The discount rates for each investment are refined to reflect the UK rate of inflation.

On 9 December 2019, the High Court of Justice formally sanctioned the Banking Business Transfer Scheme (including the acceptance of deposits), the provision of financial services and other related activities from HSBC Private Bank (UK) Limited to HSBC UK Bank plc under Part VII of the Financial Services and Markets Act 2000 for an effective date of 1 January 2020. An impairment of £483m was recognised on HSBC UK Bank plc's investment in HSBC Private Bank (UK) Limited on 31 December 2019, with there being no outstanding items at 31 December 2019 that would prevent the transfer occurring. The impairment arose because the cost of investment was higher than the consideration received for the net assets being transferred.

No impairment was recognised as a result of the impairment test performed in 2018.

14 Structured entities

The group is involved with both consolidated and unconsolidated structured entities through the securitisation of financial assets and investment funds, established either by the group or a third party.

Consolidated structured entities

Total assets of the group's consolidated structured entities, split by entity type:

	Securitisations £m	Total £m
At 31 Dec 2019	**397**	**397**
At 31 Dec 2018	–	–

Securitisations

In 2019, the group established a structured entity to securitise customer loans and advances in order to diversify its sources of funding for asset origination and capital efficiency purposes. The loans and advances were transferred by the group to the structured entity synthetically, and the structured entity issued debt securities to investors.

Unconsolidated structured entities

The term 'unconsolidated structured entities' refers to all structured entities not controlled by the group. The group enters into transactions with unconsolidated structured entities in the normal course of business to facilitate customer transactions and for specific investment opportunities.

The group's interest in unconsolidated structured entities consist of unit holdings in four funds managed by a third party within the wider HSBC Group. The groups unit holdings are held in order to facilitate customer transactions and are recognised as Other assets with a carrying value and maximum exposure to loss as at 31 December 2019 of £0.2m (2018: £0.2m). The total assets of the funds as at 31 December 2019 was £1.3bn (2018: £1.2bn). The group has no liabilities or commitments in respect of the funds.

15 Goodwill and intangible assets

	The group		The bank	
	2019 £m	2018 £m	**2019 £m**	2018 £m
Goodwill	**3,285**	3,285	**223**	223
Other intangible assets[1, 2]	**688**	525	**658**	495
At 31 Dec	**3,973**	3,810	**881**	718

1 For 2019, the amortisation and impairment of intangible assets totalled for the group £156m (2018: £64m).
2 Included within the group's other intangible assets is internally generated software with a net carrying value of £688m (2018: £518m).

Impairment testing

The group's impairment test in respect of goodwill allocated to each cash generating unit ('CGU') is performed as at 1 July each year, with a review for indicators of impairment at 30 June and 31 December. At 31 December 2019, the review identified an indicator of impairment for PB. As a result, an impairment test has been performed as at 31 December 2019 for the PB CGU. For all other CGUs, the annual test performed as at 1 July remains the latest impairment test and the disclosures given are as at 1 July for CMB and RBWM, and 31 December for PB. The testing at 1 July and 31 December resulted in no impairment of goodwill.

Basis of the recoverable amount

The recoverable amount of all CGUs to which goodwill has been allocated was equal to its value in use ('VIU') at each respective testing date for 2019 and 2018. For each CGU, the VIU is calculated by discounting management's cash flow projections for the CGU. The key assumptions used in the VIU calculation for each CGU are discussed below.

Key assumptions in VIU calculation

Cash-generating unit	Goodwill at 31 Dec 2019 £m	Discount rate %	Growth rate beyond initial cash flow projections %	Goodwill at 1 Jul 2019 £m	Discount rate %	Nominal growth rate beyond initial cash flow projections %	Goodwill at: 1 Jul 2018 £m	Discount rate %	Nominal growth rate beyond initial cash flow projections %
RBWM	**1,686**	**N/A**	**N/A**	**1,686**	**8.3**	**3.3**	1,686	7.9	3.8
CMB	**1,239**	**N/A**	**N/A**	**1,239**	**9.7**	**3.3**	1,239	9.7	3.8
PB	**360**	**8.8**	**1.8**	**360**	**9.5**	**3.3**	360	9.4	3.8
Total	**3,285**			**3,285**			3,285		

The group's CGUs do not carry on their balance sheets any significant intangible assets with indefinite useful lives, other than goodwill.

Management's judgement in estimating the cash flows of a CGU

The cash flow projections for each CGU are based on the latest plans presented to the Board. The Board challenge and endorse planning assumptions in light of internal capital allocation decisions necessary to support HSBC UK's strategy, current market conditions, and our macro-economic outlook. For the goodwill impairment tests conducted at 1 July 2019 and 31 December 2019, management's cash flow projections until the end of 2023 and 2024 were used respectively.

Discount rate

The rate used to discount the cash flows is based on the cost of capital assigned to each CGU, which is derived using a CAPM. CAPM depends on a number of inputs reflecting financial and economic variables, including the risk-free rate and a premium to reflect the inherent risk of the business being evaluated. These variables are based on the market's assessment of the economic variables and management's judgement.

Long-term growth rate

The long-term growth rate is used to extrapolate the cash flows in perpetuity because of the long-term perspective within the group of business units making up the CGUs. Prior to the 31 December impairment test, these growth rates reflected GDP and inflation (nominal GDP) for the UK. At 31 December 2019, we considered the extent to which growth rates based on nominal GDP data remained appropriate given the uncertainty in the macroeconomic environment. We anticipate that when global growth does stabilise it will be at a slightly lower level than recent years. As a result, we considered it appropriate to base the long-term growth rate assumption on inflation data, moving away from a higher nominal GDP basis. The rates are based on 20-year forecast rates, as they represent an objective estimate of likely future trends.

Sensitivities of key assumptions in calculating VIU

At 31 December 2019, the PB CGU was sensitive to reasonably possible adverse changes in the key assumptions supporting the recoverable amount. In making an estimate of reasonably possible changes to assumptions, management considers the available evidence in respect of each input to the model. These include the external range of observable discount rates, historical performance against forecast and risks attaching to the key assumptions underlying cash flow projections.

A reasonable change in a single key assumption may not result in impairment. Though taken together a combination of reasonable changes in key assumptions could result in a recoverable amount that is lower than the CGUs carrying amount.

The following table presents a summary of the key assumptions underlying the most sensitive inputs to the model for PB, the key risks attaching to each, and details of a reasonably possible change to assumptions where, in the opinion of management, these could result in an impairment.

Reasonably possible changes in key assumptions

Cash-generating unit	Input	Key assumptions	Associated risks	Reasonable possibly change
PB	Cash flow projections	• Level of interest rates. • Global Investment and UK Real Estate markets. • Assets under management growth from new business and market performance.	• Market uncertainty. • Low interest rate environment. • Regulatory changes.	• Cash flow projections decrease by 30%.
	Discount rate	• Discount rate used is a reasonable estimate of a suitable market rate for the profile of the business.	• External evidence arises to suggest that the rate used is not appropriate to the business.	• Discount rate increases by 200 basis points.

Sensitivity of VIU changes to current assumptions to achieve nil headroom

			Increase / (decrease)	
Cash-generating unit	**Carrying amount**	**Value in use**	**Discount rate**	**Cash flows**
At 31 December 2019	**£m**	**£m**	**bps**	**%**
PB	**971**	**1,189**	**200**	**(23.4)**

Whilst there are no indicators of impairment at 31 December 2019, PB's recoverable amount exceeds the carrying amount by only £218m and therefore, the test is sensitive to the assumptions used. The reasonably possible changes in assumptions for Cash Flow projections and Discount Rate, detailed above would result in an impairment. Thus there is a risk of impairment in the future should business performance or economic factors diverge from forecasts.

16 Prepayments, accrued income and other assets

	The group		The bank	
	2019 £m	2018 £m	**2019 £m**	2018 £m
Prepayments and accrued income	**740**	650	**727**	636
Settlement accounts	**16**	56	**16**	268
Cash collateral and margin receivables	**107**	279	**107**	279
Endorsements and acceptances	**71**	86	**71**	86
Employee benefit assets (Note 3)	**5,836**	5,841	**5,836**	5,841
Right-of-use assets[1]	**311**	N/A	**292**	N/A
Other accounts	**530**	1,008	**691**	921
Owned property, plant and equipment	**592**	608	**476**	492
At 31 Dec	**8,203**	8,528	**8,216**	8,523

1 Right-of-use assets have been recognised from 1 January 2019 following the adoption of IFRS 16. Comparatives have not been restated.

Prepayments, accrued income and other assets include £1,364m (2018: £2,016m) of financial assets, the majority of which are measured at amortised cost.

17 Debt securities in issue

During 2019, we have established our Debt Issuance Programme to diversify our funding sources and ensure we have appropriate access to markets.

Our Commercial Paper and Certificates of Deposit Programme was established prior to 31 December 2018 and we commenced issuing under the programme during 2019.

Debt securities in issue

	The group		The bank	
	2019 £m	2018 £m	**2019 £m**	2018 £m
Bonds and medium-term notes[1]	**1,225**	–	**1,000**	–
Other debt securities in issue[2]	**1,917**	–	**1,917**	–
Total debt securities in issue	**3,142**	–	**2,917**	–

1 The group's Bonds and medium-term notes includes £225m issued by structured entities.
2 Other debt securities in issue consists of commercial paper and certificates of deposits issued in 2019.

18 Accruals, deferred income and other liabilities

	The group		The bank	
	2019 £m	2018 £m	**2019 £m**	2018 £m
Accruals and deferred income	**562**	498	**483**	438
Settlement accounts	**14**	31	**14**	548
Cash collateral and margin payable	**13**	4	**13**	4
Endorsements and acceptances	**71**	86	**71**	86
Lease liabilities	**326**	N/A	**307**	N/A
Other liabilities	**848**	1,790	**1,383**	1,198
At 31 Dec	**1,834**	2,409	**2,271**	2,274

For the group, accruals, deferred income and other liabilities include £1,395m (2018: £2,208m), and for the bank £1,917m (2018: £2,200m) of financial liabilities, the majority of which are measured at amortised cost.

19 Provisions

The group	Restructuring costs[2] £m	Legal proceedings and regulatory matters £m	Customer remediation[3] £m	Other provisions £m	Total £m
Provisions (excluding contractual commitments)					
At 1 Jan 2019	–	–	540	5	545
Additions	59	–	1,297	–	1,356
Amounts utilised	(8)	–	(643)	–	(651)
Unused amounts reversed	–	(3)	(4)	(1)	(8)
Exchange and Other movements	1	7	–	–	8
At 31 Dec 2019	52	4	1,190	4	1,250
Contractual commitments[1]					
At 1 Jan 2019					85
Net change in expected credit loss provision and other movements					(10)
At 31 Dec 2019					75
Total provisions					
At 31 Dec 2018					630
At 31 Dec 2019					1,325
Provisions (excluding contractual commitments)					
At 1 Jan 2018	–	–	–	–	–
Transfer from HSBC Bank plc and its subsidiaries	2	2	742	5	751
Additions	–	–	78	3	81
Amounts utilised	–	–	(283)	–	(283)
Unused amounts reversed	(2)	(1)	(13)	(2)	(18)
Unwinding of discounts	–	–	–	(1)	(1)
Exchange and Other movements	–	(1)	16	–	15
At 31 Dec 2018	–	–	540	5	545
Contractual commitments[1]					
At 1 Jan 2018					–
Transfer from HSBC Bank plc and its subsidiaries					72
Net change in expected credit loss provision and other movements					13
At 31 Dec 2018					85
Total provisions					
At 31 Dec 2018					630

1 *Contractual commitments include the provision for contingent liabilities measured under IFRS 9 Financial Instruments in respect of financial guarantees and the expected credit loss provision on off-balance sheet guarantees and commitments.*
2 *Restructuring costs include charges received from HSBC Global Services (UK) Limited, which do not form part of the balance sheet provision movement.*
3 *During 2019 the additional provisions of £1,297m were recorded in the consolidated income statement under net income income (£138m), net fee income (£44m) and operating expenses (£1,115m).*

The bank	Restructuring costs[2] £m	Legal proceedings and regulatory matters £m	Customer remediation[3] £m	Other provisions £m	Total £m
Provisions (excluding contractual commitments)					
At 1 Jan 2019	–	–	427	4	431
Additions	58	–	1,054	–	1,112
Amounts utilised	(8)	–	(495)	–	(503)
Unused amounts reversed	–	(3)	(4)	–	(7)
Exchange and Other movements	1	7	1	–	9
At 31 Dec 2019	51	4	983	4	1,042
Contractual commitments[1]					
At 1 Jan 2019					84
Net change in expected credit loss provision and other movements					(12)
At 31 Dec 2019					72
Total provisions					
At 31 Dec 2018					515
At 31 Dec 2019					1,114

	Restructuring costs[2]	Legal proceedings and regulatory matters	Customer remediation	Other provisions	Total
Provisions (excluding contractual commitments)					
At 1 Jan 2018	–	–	–	–	–
Transfer from HSBC Bank plc and its subsidiaries	2	–	615	5	622
Additions	–	–	18	2	20
Amounts utilised	–	–	(209)	–	(209)
Unused amounts reversed	(2)	–	(13)	(2)	(17)
Unwinding of discounts	–	–	–	(1)	(1)
Exchange and Other movements	–	–	16	–	16
At 31 Dec 2018	–	–	427	4	431
Contractual commitments[1]					
At 1 Jan 2018					–
Transfer from HSBC Bank plc					71
Net change in expected credit loss provision and other movements					13
At 31 Dec 2018					84
Total provisions					
At 31 Dec 2018					515

1 *Contractual commitments include the provision for contingent liabilities measured under IFRS 9 Financial Instruments in respect of financial guarantees and the expected credit loss provision on off-balance sheet guarantees and commitments.*
2 *Restructuring costs include charges received from HSBC Global Services (UK) Limited, which do not form part of the balance sheet provision movement.*
3 *During 2019 the additional provisions of £1,054m were recorded in the HSBC UK income statement under net income income (£126m), net fee income (£32m) and operating expenses (£896m).*

Payment Protection Insurance

At 31 December 2019, £801m (2018: £435m) of the customer remediation provision relates to the estimated liability for redress in respect of the possible mis-selling of payment protection insurance ('PPI') policies in previous years.

Payments totalling £567m were made during 2019. An increase in provisions of £932m was recognised during the year, primarily reflecting the deadline of 29 August 2019 for bringing complaints announced by the FCA, and leading to:

- a higher than expected increase in the number of inbound complaints received prior to 29 August 2019;
- The effect on the total number of inbound complaints as a result of treating customer information requests relating to PPI policies received between 29 June 2019 and 29 August 2019 as complaints;
- the additional operational expenses related to the increases in populations of potential claims;
- an industry wide exercise by the Official Receiver to pursue redress amounts in respect of bankrupt and insolvent customers; and
- an increased volume of actual or forecast legal claims for PPI mis-selling which is not affected by the deadline of 29 August 2019.

The estimated liability for redress for both single and regular premium policies is calculated on the basis of a refund of the total premiums paid by the customer plus simple interest of 8% per annum (or the rate inherent in the related loan product where higher).

Future estimated redress levels are based on historical redress paid to customers per policy.

At 31 December 2019, contact has been made with customers who collectively held 3.0 million policies, representing 56% of total policies sold. A total of 5.4 million PPI policies have been sold since 2000, generating estimated revenue of £2.6bn at 2019. The gross written premiums on these policies were approximately £3.4bn. Although the deadline for bringing complaints has passed, customers can still commence litigation for PPI mis-selling. Provision has been made for the best estimate of any obligation to pay compensation in respect of an estimated 45,000 claims. However, given the limited period following the complaints time bar, the volume and quality of future claims through legal channels, and the amount of any compensation to be paid, remain uncertain.

The following table summarises the cumulative number of information requests received between 29 June to 29 August 2019, and the number of claims expected to be assessed in the future, excluding claims received through legal channels:

Cumulative PPI complaints received to 31 December 2019

	Cumulative actual to 31 Dec 2019
Information Requests received during Autoconversion period (000s)	1,889
Information Requests awaiting evaluation (000s)	234
Remaining autoconverted claims anticipated to be worked (000s)[1]	167
Remaining reactive claims anticipated to be worked (000s)[1]	44
Total remaining claims anticipated to be worked (000s)[1]	211
Average uphold rate per claim[2]	86%
Average redress per claim[3] (£)	2,440

1 *Includes claims where a valid PPI policy had already been located, and claims which are anticipated to be valid after future assessment; excludes invalid claims for which no PPI policy exists.*
2 *Includes inbound and auto-converted claims, but excludes Financial Ombudsman Service complaints.*
3 *Includes inbound and auto-converted claims, but excludes claims from the Official Receiver.*

The PPI provision is based upon assumptions and estimates taken from historic experience. The profile of cases yet to be assessed could therefore vary leading to different uphold rates or average redress levels being used to arrive at the provision.

We continued to monitor available information up until the date of the approval of the financial statements to ensure the provision estimate was appropriate.

Sensitivity to key assumptions

- A 10% increase/decrease in the uphold rate for complaints yet to be worked would increase/decrease the redress provision by approximately £30m.
- A 10% increase/decrease in the average redress for complaints yet to be worked would increase/decrease the redress provision by approximately £42m.
- An increase/decrease in customer redress volumes of 10,000 received through legal channels would increase/decrease the redress provision by approximately £22m.

Collections and recoveries related matters

At 31 December 2019, a provision of £220m was held relating to the estimated liability for redress payable to customers following a review of collections and recoveries practices in the UK in respect of various HSBC Group companies, including HSBC UK.

The provision has been estimated based on a number of customer cohorts who may have been impacted and a number of assumptions which are highly judgemental, none of which are individually material. At this early stage, the extraction of all relevant data is incomplete, and there is significant uncertainty surrounding the total number of customers affected and the amount of any redress to be paid. Redress is expected to be completed during 2020.

The table below sets out sensitivities to the assumptions applied but it is not intended to indicate a range of any final amount payable.

Assumption	£m
20% increase/decrease in population of customers impacted	**40.4**
20% increase/decrease in level of redress to be paid in respect of interest and fees charged	**26.6**

Customer fee and mischarging related matters

At 31 December 2019, £118m of the customer remediation provision relates to the estimated liability for redress in respect of customer fee and mischarging related matters. This follows internal reviews to identify any issues for which provisions had not previously been raised and to re-assess provisions in respect of matters previously provided for.

As a consequence of the matters identified from these reviews, additional provisions of £117m were recognised in the period. The provision relates to a number of different issues, none of which are individually material.

The estimated liability for redress is based on sampling and analysis performed to date for each of the matters, detailed reviews to identify exact populations requiring redress are ongoing and expect to be completed in 2020.

Legal proceedings and regulatory matters

Further details of legal proceedings and regulatory matters are set out in Note 26. Legal proceedings include civil court, arbitration or tribunal proceedings brought against the group (whether by way of claim or counterclaim), or civil disputes that may, if not settled, result in court, arbitration or tribunal proceedings. Regulatory matters refer to investigations, reviews and other actions carried out by, or in response to the actions of, regulatory or law enforcement agencies in connection with alleged wrongdoing.

20 Subordinated liabilities

Subordinated liabilities

	The group		The bank	
	2019 £m	2018 £m	**2019 £m**	2018 £m
At amortised cost	**9,533**	4,937	**9,454**	4,858
– subordinated liabilities[1]	**9,533**	4,937	**9,454**	4,858
At 31 Dec	**9,533**	4,937	**9,454**	4,858

1 *Includes £6.5bn of eligible debt issued to meet our Minimum requirement for own funds and Eligible Liabilities ('MREL') applicable from 1 January 2020.*

Subordinated liabilities rank behind senior obligations and generally count towards the capital base of the group. Capital securities may be called and redeemed by the group subject to prior notification to and consent of the PRA.

The balance sheet amounts disclosed below are presented on an IFRS basis and do not reflect the amount that the instruments contribute to regulatory capital principally due to regulatory amortisation and regulatory eligibility limits.

Subordinated liabilities of the group

		First call date	Maturity date	Carrying amount 2019 £m	Carrying amount 2018 £m
Capital instruments					
Tier 2 instruments					
£550m	HSBC UK Bank plc Subordinated Floating Loan 2028[1]	Jul 2023	Jul 2028	**550**	550
£1,000m	HSBC UK Bank plc Subordinated Floating Loan 2030[2]	Jul 2025	Jul 2030	**1,000**	1,000
£650m	HSBC UK Bank plc Subordinated Floating Loan 2033[3]	Sep 2028	Sep 2033	**650**	650
$840m	HSBC UK Bank plc Subordinated Floating Loan 2028[5]	Jul 2023	Jul 2028	**635**	658
£100m	HSBC UK Bank plc 2.8594% Subordinated Loan 2029	Mar 2024	Mar 2029	**100**	–
Other Tier 2 instruments each less that £100m[4]				**79**	79
Other instruments					
Subordinated loan instruments not eligible for inclusion in regulatory capital					
£1,000m	HSBC UK Bank plc 3.2485% MREL eligible Subordinated Loan 2026	Nov 2025	Nov 2026	**1,000**	1,000
£1,000m	HSBC UK Bank plc 3.4602% MREL eligible Subordinated Loan 2029	Aug 2028	Aug 2029	**1,000**	1,000
£1,000m	HSBC UK Bank plc 3.0000% MREL eligible Subordinated Loan 2028	Jul 2027	Jul 2028	**1,000**	–
$3000m	HSBC UK Bank plc 3.9730% MREL eligible Subordinated Loan 2030	May 2029	May 2030	**2,269**	–
£750m	HSBC UK Bank plc 3.0000% MREL eligible Subordinated Loan 2030	May 2029	May 2030	**750**	–
£350m	HSBC UK Bank plc 1.8777% MREL eligible Subordinated Loan 2025	Oct 2024	Oct 2025	**350**	–
£150m	HSBC UK Bank plc 2.1003% MREL eligible Subordinated Loan 2025	Oct 2024	Oct 2025	**150**	–
At 31 Dec				**9,533**	4,937

1 The distribution rate is three month sterling Libor plus 1.51%.
2 The distribution rate is three month sterling Libor plus 1.78%.
3 The distribution rate is three month sterling Libor plus 2.03%.
4 Two subordinated notes issued by Marks and Spencer Financial Services plc, £54m maturing 2026 and £25m maturing 2027.
5 The distribution rate is three month USD Libor plus 1.51%.

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

The following table provides an analysis of consolidated total assets, liabilities and off-balance sheet commitments by residual contractual maturity at the balance sheet date. These balances are included in the maturity analysis as follows:

- Trading derivatives are included in the 'Due not more than 1 month' time bucket, because trading balances are typically held for short periods of time.
- Financial assets and liabilities with no contractual maturity (such as equity securities) are included in the 'Due over 5 years' time bucket. Undated or perpetual instruments are classified based on the contractual notice period which the counterparty of the instrument is entitled to give. Where there is no contractual notice period, undated or perpetual contracts are included in the 'Due over 5 years' time bucket.
- Non-financial assets and liabilities with no contractual maturity are included in the 'Due over 5 years' time bucket.
- Loan and other credit-related commitments are classified on the basis of the earliest date they can be drawn down.

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

	Due not more than 1 month	Due over 1 month but not more than 3 months	Due over 3 months but not more than 6 months	Due over 6 months but not more than 9 months	Due over 9 months but not more than 1 year	Due over 1 year but not more than 2 years	Due over 2 years but not more than 5 years	Due over 5 years	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
The group									
Financial assets									
Cash and balances at central banks	37,030	–	–	–	–	–	–	–	37,030
Items in the course of collection from other banks	504	–	–	–	–	–	–	–	504
Financial assets designated or otherwise mandatorily measured at fair value	57	–	–	–	–	–	–	9	66
Derivatives	63	1	3	2	–	2	8	42	121
Loans and advances to banks	786	–	603	–	–	–	–	–	1,389
Loans and advances to customers	20,484	10,827	7,576	5,774	5,240	17,685	30,911	84,559	183,056
– personal	5,834	4,776	1,839	1,702	1,636	6,216	16,657	78,271	116,931
– corporate and commercial	14,073	5,772	5,461	3,906	3,466	11,003	13,753	6,170	63,604
– financial	577	279	276	166	138	466	501	118	2,521
Reverse repurchase agreements – non-trading	1,671	1,260	83	–	–	–	–	–	3,014
Financial investments	317	1,603	2,085	1,471	227	1,309	6,800	5,925	19,737
Accrued income and other financial assets	1,143	118	27	8	7	39	22	–	1,364
Total financial assets at 31 Dec 2019	62,055	13,809	10,377	7,255	5,474	19,035	37,741	90,535	246,281
Non-financial assets	–	–	–	–	–	–	–	10,821	10,821
Total assets at 31 Dec 2019	62,055	13,809	10,377	7,255	5,474	19,035	37,741	101,356	257,102
Financial liabilities									
Deposits by banks	513	16	–	–	–	–	–	–	529
Customer accounts[1]	211,409	2,401	510	428	539	440	487	–	216,214
– personal	136,192	860	440	400	462	435	485	–	139,274
– corporate and commercial	70,125	1,443	59	27	77	4	2	–	71,737
– financial	5,092	98	11	1	–	1	–	–	5,203
Repurchase agreements – non-trading	98	–	–	–	–	–	–	–	98
Items in the course of transmission to other banks	343	–	–	–	–	–	–	–	343
Derivatives	67	–	–	1	1	3	56	73	201
Debt securities in issue	483	566	868	1,000	–	–	–	225	3,142
Accruals and other financial liabilities	1,223	181	25	17	17	64	120	74	1,721
Subordinated liabilities	–	–	–	–	–	–	–	9,533	9,533
Total financial liabilities at 31 Dec 2019	214,136	3,164	1,403	1,446	557	507	663	9,905	231,781
Non-financial liabilities	–	–	–	–	–	–	–	3,070	3,070
Total liabilities at 31 Dec 2019	214,136	3,164	1,403	1,446	557	507	663	12,975	234,851
Off-balance sheet commitments given									
Loan and other credit-related	67,118	4	1	2	7	114	41	15	67,302
– personal	37,014	–	–	–	–	–	–	–	37,014
– corporate and commercial	28,600	4	1	2	7	114	41	15	28,784
– financial	1,504	–	–	–	–	–	–	–	1,504

Maturity analysis of assets, liabilities and off-balance sheet commitments (continued)

	Due not more than 1 month	Due over 1 month but not more than 3 months	Due over 3 months but not more than 6 months	Due over 6 months but not more than 9 months	Due over 9 months but not more than 1 year	Due over 1 year but not more than 2 years	Due over 2 years but not more than 5 years	Due over 5 years	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
The group									
Financial assets									
Cash and balances at central banks	33,193	–	–	–	–	–	–	–	33,193
Items in the course of collection from other banks	603	–	–	–	–	–	–	–	603
Financial assets designated or otherwise mandatorily measured at fair value	29	–	–	–	–	–	–	6	35
Derivatives	50	–	9	–	–	6	–	1	66
Loans and advances to banks	908	–	351	–	–	–	–	4	1,263
Loans and advances to customers	14,085	9,321	7,562	5,918	5,676	18,257	33,511	80,477	174,807
– personal	2,415	1,546	2,164	2,143	2,040	7,363	17,843	74,129	109,643
– corporate and commercial	10,917	7,566	5,173	3,622	3,396	10,627	15,163	6,167	62,631
– financial	753	209	225	153	240	267	505	181	2,533
Reverse repurchase agreements – non-trading	1,989	1,433	–	–	–	–	–	–	3,422
Financial investments	375	444	1,024	518	568	393	6,366	3,515	13,203
Accrued income and other financial assets	1,805	182	26	2	1	–	–	–	2,016
Total financial assets at 31 Dec 2018	53,037	11,380	8,972	6,438	6,245	18,656	39,877	84,003	228,608
Non-financial assets	–	–	–	–	–	–	–	10,331	10,331
Total assets at 31 Dec 2018	53,037	11,380	8,972	6,438	6,245	18,656	39,877	94,334	238,939
Financial liabilities									
Deposits by banks	1,018	9	–	–	–	–	–	–	1,027
Customer accounts[1]	200,036	2,103	1,023	692	528	312	134	9	204,837
– personal	128,872	873	816	657	477	297	122	7	132,121
– corporate and commercial	66,700	1,054	188	34	50	15	12	2	68,055
– financial	4,464	176	19	1	1	–	–	–	4,661
Repurchase agreements – non-trading	189	–	450	–	–	–	–	–	639
Items in the course of transmission to other banks	233	–	–	–	–	–	–	–	233
Derivatives	44	3	–	26	–	134	–	139	346
Debt securities in issue	–	–	–	–	–	–	–	–	–
Accruals and other financial liabilities	1,671	399	14	–	–	–	–	94	2,178
Subordinated liabilities	–	–	–	–	–	–	–	4,937	4,937
Total financial liabilities at 31 Dec 2018	203,191	2,514	1,487	718	528	446	134	5,179	214,197
Non-financial liabilities	–	–	–	–	–	–	–	2,409	2,409
Total liabilities at 31 Dec 2018	203,191	2,514	1,487	718	528	446	134	7,588	216,606
Off-balance sheet commitments given									
Loan and other credit-related	69,570	13	–	42	–	78	59	44	69,806
– personal	39,389	–	–	–	–	–	–	–	39,389
– corporate and commercial	29,895	13	–	42	–	78	59	44	30,131
– financial	286	–	–	–	–	–	–	–	286

1 *'Customers accounts' includes £114,056m (2018: £110,226m) insured by guarantee schemes.*

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

	Due not more than 1 month	Due over 1 month but not more than 3 months	Due over 3 months but not more than 6 months	Due over 6 months but not more than 9 months	Due over 9 months but not more than 1 year	Due over 1 year but not more than 2 years	Due over 2 years but not more than 5 years	Due over 5 years	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
The bank									
Financial assets									
Cash and balances at central banks	37,020	–	–	–	–	–	–	–	37,020
Items in the course of collection from other banks	355	–	–	–	–	–	–	–	355
Financial assets designated or otherwise mandatorily measured at fair value	57	–	–	–	–	–	–	9	66
Derivatives	60	1	3	2	–	2	8	42	118
Loans and advances to banks	1,001	476	1,308	171	149	532	964	42	4,643
Loans and advances to customers	19,016	8,079	8,799	5,428	5,012	16,673	27,475	83,419	173,901
– personal	5,102	2,018	1,496	1,410	1,413	5,514	14,958	77,782	109,693
– corporate and commercial	11,490	3,910	4,608	3,708	3,307	10,142	11,254	5,459	53,878
– financial	2,424	2,151	2,695	310	292	1,017	1,263	178	10,330
Reverse repurchase agreements – non-trading	1,671	1,260	83	–	–	–	–	–	3,014
Financial investments	317	1,603	2,085	1,471	227	1,309	6,800	5,925	19,737
Accrued income and other financial assets	1,413	84	20	1	1	–	–	–	1,519
Total financial assets at 31 Dec 2019	60,910	11,503	12,298	7,073	5,389	18,516	35,247	89,437	240,373
Non-financial assets	–	–	–	–	–	–	–	9,183	9,183
Total assets at 31 Dec 2019	60,910	11,503	12,298	7,073	5,389	18,516	35,247	98,620	249,556
Financial liabilities									
Deposits by banks	4,024	36	46	35	32	60	44	–	4,277
Customer accounts[1]	203,400	2,092	452	428	531	440	487	–	207,830
– personal	130,290	617	391	400	455	436	485	–	133,074
– corporate and commercial	69,419	1,380	50	27	76	4	2	–	70,958
– financial	3,691	95	11	1	–	–	–	–	3,798
Repurchase agreements – non-trading	98	–	–	–	–	–	–	–	98
Items in the course of transmission to other banks	336	–	–	–	–	–	–	–	336
Derivatives	62	–	–	1	1	3	56	74	197
Debt securities in issue	483	566	868	1,001	–	–	–	–	2,918
Accruals and other financial liabilities	1,778	149	23	16	16	60	109	74	2,225
Subordinated liabilities	–	–	–	–	–	–	–	9,454	9,454
Total financial liabilities at 31 Dec 2019	210,181	2,843	1,389	1,481	580	563	696	9,602	227,335
Non-financial liabilities	–	–	–	–	–	–	–	2,776	2,776
Total liabilities at 31 Dec 2019	210,181	2,843	1,389	1,481	580	563	696	12,378	230,111
Off-balance sheet commitments given									
Loan and other credit-related commitments	52,875	–	–	–	–	–	–	–	52,875
– personal	25,891	–	–	–	–	–	–	–	25,891
– corporate and commercial	26,470	–	–	–	–	–	–	–	26,470
– financial	514	–	–	–	–	–	–	–	514

Maturity analysis of assets, liabilities and off-balance sheet commitments (continued)

	Due not more than 1 month	Due over 1 month but not more than 3 months	Due over 3 months but not more than 6 months	Due over 6 months but not more than 9 months	Due over 9 months but not more than 1 year	Due over 1 year but not more than 2 years	Due over 2 years but not more than 5 years	Due over 5 years	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
The bank									
Financial assets									
Cash and balances at central banks	33,187	–	–	–	–	–	–	–	33,187
Items in the course of collection from other banks	457	–	–	–	–	–	–	–	457
Financial assets designated or otherwise mandatorily measured at fair value	29	–	–	–	–	–	–	6	35
Derivatives	45	–	9	–	–	6	–	1	61
Loans and advances to banks	1,041	445	1,012	118	121	418	697	31	3,883
Loans and advances to customers	14,006	6,634	9,228	5,485	5,259	17,200	29,427	78,611	165,850
– personal	1,652	1,149	1,739	1,722	1,714	6,274	15,636	72,839	102,725
– corporate and commercial	10,338	3,397	4,353	3,433	3,144	10,021	12,498	5,538	52,722
– financial	2,016	2,088	3,136	330	401	905	1,293	234	10,403
Reverse repurchase agreements – non-trading	1,989	1,433	–	–	–	–	–	–	3,422
Financial investments	375	444	1,024	518	568	393	6,367	3,514	13,203
Accrued income and other financial assets	2,025	76	26	2	1	–	–	–	2,130
Total financial assets at 31 Dec 2018	53,154	9,032	11,299	6,123	5,949	18,017	36,491	82,163	222,228
Non-financial assets	–	–	–	–	–	–	–	9,023	9,023
Total assets at 31 Dec 2018	53,154	9,032	11,299	6,123	5,949	18,017	36,491	91,186	231,251
Financial liabilities									
Deposits by banks	3,956	39	115	50	50	25	30	–	4,265
Customer accounts[1]	193,037	1,579	810	555	509	264	104	–	196,858
– personal	123,626	480	643	529	465	257	100	–	126,100
– corporate and commercial	65,326	923	148	25	43	7	4	–	66,476
– financial	4,085	176	19	1	1	–	–	–	4,282
Repurchase agreements – non-trading	189	–	450	–	–	–	–	–	639
Items in the course of transmission to other banks	225	–	–	–	–	–	–	–	225
Derivatives	38	3	–	26	–	134	–	140	341
Debt securities in issue	–	–	–	–	–	–	–	–	–
Accruals and other financial liabilities	2,015	139	16	–	–	–	–	–	2,170
Subordinated liabilities	–	–	–	–	–	–	–	4,858	4,858
Total financial liabilities at 31 Dec 2018	199,460	1,760	1,391	631	559	423	134	4,998	209,356
Non-financial liabilities	–	–	–	–	–	–	–	2,129	2,129
Total liabilities at 31 Dec 2018	199,460	1,760	1,391	631	559	423	134	7,127	211,485
Off-balance sheet commitments given									
Loan and other credit-related commitments	55,505	–	–	–	–	–	–	–	55,505
– personal	28,009	–	–	–	–	–	–	–	28,009
– corporate and commercial	27,264	–	–	–	–	–	–	–	27,264
– financial	232	–	–	–	–	–	–	–	232

1 'Customers accounts' includes £111,797m (2018: £107,993m) insured by guarantee schemes.

Contractual maturity of financial liabilities

The table below shows, on an undiscounted basis, all cash flows relating to principal and future coupon payments (except for derivatives not treated as hedging derivatives). For this reason, balances in the table below do not agree directly with those in our consolidated balance sheet and the bank's balance sheet. Undiscounted cash flows payable in relation to hedging derivative liabilities are classified according to their contractual maturities. Derivatives not treated as hedging derivatives are included in the 'Due not more than 1 month' time bucket and not by contractual maturity. In addition, loans and other credit-related commitments, financial guarantees and similar contracts are generally not recognised on our balance sheet. The undiscounted cash flows potentially payable under loan and other credit-related commitments, and financial guarantees are classified on the basis of the earliest date they can be called.

Cash flows payable under financial liabilities by remaining contractual maturities

The group	Due not more than 1 month	Due over 1 month but not more than 3 month	Due over 3 month but not more than 1 year	Due over 1 year but not more than 5 years	Due over 5 years	Total
	£m	£m	£m	£m	£m	£m
Deposits by banks	**505**	**24**	**–**	**–**	**–**	**529**
Customer accounts	**206,683**	**7,132**	**1,488**	**941**	**–**	**216,244**
Repurchase agreements – non-trading	**–**	**99**	**–**	**–**	**–**	**99**
Derivatives	**67**	**27**	**31**	**208**	**255**	**588**
Debt securities in issue	**–**	**1,233**	**1,973**	**103**	**277**	**3,586**
Subordinated liabilities	**–**	**77**	**232**	**1,225**	**12,595**	**14,129**
Other financial liabilities	**1,186**	**553**	**58**	**184**	**74**	**2,055**
	208,441	**9,145**	**3,782**	**2,661**	**13,201**	**237,230**
Loan and other credit-related commitments	**67,117**	**4**	**10**	**155**	**15**	**67,301**
Financial guarantees	**1,077**	**–**	**–**	**–**	**–**	**1,077**
At 31 Dec 2019	**276,635**	**9,149**	**3,792**	**2,816**	**13,216**	**305,608**
Proportion of cash flows payable in period	**91%**	**3%**	**1%**	**1%**	**4%**	**100%**
Deposits by banks	1,018	8	–	–	–	1,026
Customer accounts	196,287	5,886	2,250	454	12	204,889
Repurchase agreements – non-trading	–	189	453	–	–	642
Derivatives	44	3	26	133	279	485
Debt securities in issue	–	–	–	–	–	–
Subordinated liabilities	–	35	105	557	6,329	7,026
Other financial liabilities	1,792	679	13	–	–	2,484
	199,141	6,800	2,847	1,144	6,620	216,552
Loan and other credit-related commitments	69,552	29	42	137	44	69,804
Financial guarantees	1,284	–	–	–	–	1,284
At 31 Dec 2018	269,977	6,829	2,889	1,281	6,664	287,640
Proportion of cash flows payable in period	95%	2%	1%	0%	2%	100%

Cash flows payable under financial liabilities by remaining contractual maturities

The bank	Due not more than 1 month	Due over 1 month but not more than 3 month	Due over 3 month but not more than 1 year	Due over 1 year but not more than 5 years	Due over 5 years	Total
	£m	£m	£m	£m	£m	£m
Deposits by banks	**2,645**	**1,419**	**115**	**110**	**–**	**4,289**
Customer accounts	**200,449**	**5,050**	**1,417**	**940**	**–**	**207,856**
Repurchase agreements – non-trading	**–**	**99**	**–**	**–**	**–**	**99**
Derivatives	**62**	**27**	**31**	**209**	**255**	**584**
Debt securities in issue	**–**	**1,227**	**1,954**	**–**	**–**	**3,181**
Subordinated liabilities	**–**	**77**	**232**	**1,225**	**12,516**	**14,050**
Other financial liabilities	**1,743**	**520**	**54**	**168**	**74**	**2,559**
	204,899	**8,419**	**3,803**	**2,652**	**12,845**	**232,618**
Loan and other credit-related commitments	**52,875**	**–**	**–**	**–**	**–**	**52,875**
Financial guarantees	**1,066**	**–**	**–**	**–**	**–**	**1,066**
At 31 Dec 2019	**258,840**	**8,419**	**3,803**	**2,652**	**12,845**	**286,559**
Proportion of cash flows payable in period	**91%**	**3%**	**1%**	**1%**	**4%**	**100%**
Deposits by banks	1,214	2,790	217	58	–	4,279
Customer accounts	190,070	4,559	1,879	373	–	196,881
Repurchase agreements – non-trading	–	189	453	–	–	642
Derivatives	38	3	26	133	279	479
Debt securities in issue	–	–	–	–	–	–
Subordinated liabilities	–	35	105	557	6,250	6,947
Other financial liabilities	2,569	411	13	–	–	2,993
	193,891	7,987	2,693	1,121	6,529	212,221
Loan and other credit-related commitments	55,505	–	–	–	–	55,505
Financial guarantees	1,263	–	–	–	–	1,263
At 31 Dec 2018	250,659	7,987	2,693	1,121	6,529	268,989
Proportion of cash flows payable in period	94%	3%	1%	0%	2%	100%

22 Offsetting of financial assets and financial liabilities

The 'Amounts not set off in the balance sheet' include transactions where:

- *the counterparty has an offsetting exposure with the group and a master netting or similar arrangement is in place with a right of set* off only in the event of default, insolvency or bankruptcy, or the offset criteria are not otherwise satisfied; and
- in the case of derivatives and reverse repurchase/repurchase, stock borrowing/lending and similar agreements, cash and non-cash collateral has been received/pledged.

For risk management purposes, the net amounts of loans and advances to customers are subject to limits, which are monitored and the relevant customer agreements are subject to review and updated, as necessary, to ensure that the legal right of offset remains appropriate.

	Amounts subject to enforceable netting arrangements								
				Amounts not set off in the balance sheet					
	Gross amounts	Amounts offset	Net amounts in the balance sheet	Financial instruments	Non-cash collateral	Cash collateral	Net amount	Amounts not subject to enforceable netting arrangements[4]	Total
	£m	£m	£m	£m	£m	£m	£m	£m	£m
Financial assets									
Derivatives[1] (Note 9)	**691**	**(573)**	**118**	**(57)**	**–**	**(7)**	**54**	**3**	**121**
Reverse repos, stock borrowing and similar agreements classified as:									
– non-trading assets	**3,697**	**(683)**	**3,014**	**–**	**(3,014)**	**–**	**–**	**–**	**3,014**
Loans and advances to customers[2]	**5,720**	**(1,326)**	**4,394**	**(3,764)**	**–**	**–**	**630**	**4**	**4,398**
At 31 Dec 2019	**10,108**	**(2,582)**	**7,526**	**(3,821)**	**(3,014)**	**(7)**	**684**	**7**	**7,533**
Derivatives[1] (Note 9)	263	(202)	61	(22)	(25)	(4)	10	5	66
Reverse repos, stock borrowing and similar agreements classified as:									
– non-trading assets	3,422	–	3,422	–	(3,422)	–	–	–	3,422
Loans and advances to customers[2]	7,768	(2,021)	5,747	(4,177)	–	–	1,570	–	5,747
At 31 Dec 2018	11,453	(2,223)	9,230	(4,199)	(3,447)	(4)	1,580	5	9,235
Financial liabilities									
Derivatives[1] (Note 9)	**770**	**(573)**	**197**	**(57)**	**–**	**(32)**	**108**	**4**	**201**
Repos, stock lending and similar agreements classified as:									
– non-trading liabilities	**781**	**(683)**	**98**	**–**	**(98)**	**–**	**–**	**–**	**98**
Customer accounts[3]	**6,936**	**(1,326)**	**5,610**	**(3,764)**	**–**	**–**	**1,846**	**4**	**5,614**
At 31 Dec 2019	**8,487**	**(2,582)**	**5,905**	**(3,821)**	**(98)**	**(32)**	**1,954**	**8**	**6,912**
Derivatives[1] (Note 9)	543	(202)	341	(22)	–	(95)	224	5	346
Repos, stock lending and similar agreements classified as:									
– non-trading liabilities	639	–	639	–	(639)	–	–	–	639
Customer accounts[3]	7,311	(2,021)	5,290	(4,177)	–	–	1,113	1	5,291
At 31 Dec 2018	8,493	(2,223)	6,270	(4,199)	(639)	(95)	1,337	6	6,276

1 *At 31 December 2019, the amount of cash margin paid that had been offset against the gross derivatives liabilities was £168m (2018: £141m).*
2 *At 31 December 2019, the total amount of 'Loans and advances to customers' recognised on the balance sheet was £183,056m (2018: £174,807m) of which £4,394m (2018: £5,747m) was subject to offsetting.*
3 *At 31 December 2019, the total amount of 'Customer accounts' recognised on the balance sheet was £216,214m (2018: £204,837m) of which £5,610m (2018: £5,290m) was subject to offsetting.*
4 *These exposures continue to be secured by financial collateral, but we may not have sought or been able to obtain a legal opinion evidencing enforceability of the right of offset.*

23 Called up share capital and other equity instruments

Called up share capital and share premium

HSBC UK Bank plc ordinary shares of £1.00 each, issued and fully paid

	2019		2018	
	Number	£m	Number	£m
At 1 Jan and 31 Dec	**50,002**	**–**	50,002	–

HSBC UK Bank plc share premium

	2019	2018
	£m	£m
At 31 Dec	**9,015**	9,015

Total called up share capital and share premium

	2019	2018
	£m	£m
At 31 Dec	**9,015**	9,015

Other equity instruments

HSBC UK Bank plc additional tier 1 instruments

		2019 £m	2018 £m
£1,096m	Undated Subordinated Additional Tier 1 instrument issued 2014 (Callable December 2019 onwards)	**1,096**	1,096
£1,100m	Undated Subordinated Additional Tier 1 instrument issued 2014 (Callable December 2024 onwards)	**1,100**	1,100
At 31 Dec		**2,196**	2,196

The bank has issued capital instruments that are included in the group's capital base as fully CRD IV compliant additional tier 1 capital.

Interest on these instruments will be due and payable only at the sole discretion of the bank, and the bank has sole and absolute discretion at all times and for any reason to cancel (in whole or in part) any interest payment that would otherwise be payable on any date. There are limitations on the payment of principal, interest or other amounts if such payments are prohibited under UK banking regulations, or other requirements, if the bank has insufficient distributable items or if the bank fails to satisfy the solvency condition as defined in the instruments terms.

The instruments are undated and are repayable, at the option of the bank, in whole at the initial call date, or on any Interest Payment Date after the initial call date. In addition, the instruments are repayable at the option of the bank in whole for certain regulatory or tax reasons. Any repayments require the prior notification to and consent of the PRA. These instruments rank *pari passu* with the bank's most senior class or classes of issued preference shares and therefore ahead of ordinary shares. These instruments will be written down in whole, together with any accrued but unpaid interest if either the group's solo or consolidated Common Equity Tier 1 Capital Ratio falls below 7.00%.

24 Contingent liabilities, contractual commitments and guarantees

	The group		The bank	
	2019 £m	2018 £m	**2019 £m**	2018 £m
Guarantees and other contingent liabilities:				
– financial guarantees[1]	**1,077**	1,284	**1,066**	1,263
– performance and other guarantees	**2,351**	2,220	**2,351**	2,220
At 31 Dec	**3,428**	3,504	**3,417**	3,483
Commitments[2]:				
– documentary credits and short-term trade-related transactions	**95**	83	**95**	83
– forward asset purchases and forward deposits placed	**184**	248	**–**	–
– standby facilities, credit lines and other commitments to lend	**67,023**	69,475	**52,780**	55,422
At 31 Dec	**67,302**	69,806	**52,875**	55,505

1 *Financial guarantees contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss incurred because a specified debtor fails to make payment when due, in accordance with the original or modified terms of a debt instrument. The amounts in the above table are nominal principal amounts.*

2 *Includes £64bn of commitments at 31 December 2019, (2018:£65bn) to which the impairment requirements in IFRS 9 are applied where the group has become party to an irrevocable commitment.*

The above table discloses the nominal principal amounts, which represents the maximum amounts at risk should the contracts be fully drawn upon and clients default. As a significant portion of guarantees and commitments is expected to expire without being drawn upon, the total of the nominal principal amounts is not indicative of future liquidity requirements. The expected credit loss provision relating to guarantees and commitments under IFRS 9 is disclosed in Note 19.

The majority of the guarantees have a term of less than one year, while guarantees of more than one year are subject the group's annual credit review process.

Contingent liabilities arising from legal proceedings, regulatory and other matters against group companies are disclosed in Note 26

Financial Services Compensation Scheme

The Financial Services Compensation Scheme ('FSCS') provides compensation to customers of financial services firms that have failed. Following the Financial Crisis, the compensation paid out to customers was initially funded through loans from HM Treasury which was fully repaid in 2018 by the FSCS. HSBC UK could be liable to pay a proportion of any future amounts that the FSCS borrows from HM Treasury to the extent the industry levies imposed to date are not sufficient to cover the compensation due to customers in any future possible collapse. The ultimate FSCS levy to the industry as a result of a collapse cannot be estimated reliably. It is dependent on various uncertain factors including the potential recovery of assets by the FSCS, changes in the level of protected products (including deposits and investments) and the population of FSCS members at the time.

The group provides guarantees and similar undertakings on behalf of third-party customers. These guarantees are generally provided in the normal course of the group's banking businesses.

25 Lease commitments

Finance lease receivables

The group leases a variety of assets to third parties under finance leases, including transport assets, property and general plant and machinery. At the end of lease terms, assets may be sold to third parties or leased for further terms. Rentals are calculated to recover the cost of assets less their residual value, and earn finance income.

	2019			2018		
	Total future minimum payments	**Unearned finance income**	**Present Value**	Total future minimum payments	Unearned finance income	Present Value
	£m	**£m**	**£m**	£m	£m	£m
Lease receivables						
– No later than one year	**33**	**(5)**	**28**	588	(35)	553
– Later than one year and no later than 5 years	**N/A**	**N/A**	**N/A**	2,716	(155)	2,561
– One to two years[1]	**341**	**(19)**	**322**	N/A	N/A	N/A
– Two to three years[1]	**607**	**(32)**	**575**	N/A	N/A	N/A
– Three to four years[1]	**635**	**(33)**	**602**	N/A	N/A	N/A
– Four to five years[1]	**713**	**(36)**	**677**	N/A	N/A	N/A
– Later than 5 years	**1,469**	**(81)**	**1,388**	707	(52)	655
At 31 Dec	**3,798**	**(206)**	**3,592**	4,011	(242)	3,769

1 For 2019 additional maturity bandings have been presented as required under IFRS 16, 2018 maturity bandings have not been restated.

26 Legal proceedings and regulatory matters

The group is party to legal proceedings and regulatory matters in a number of jurisdictions arising out of its normal business operations. Apart from the matters described below, the group considers that none of these matters are material. The recognition of provisions is determined in accordance with the accounting policies set out in Note 1. While the outcome of legal proceedings and regulatory matters is inherently uncertain, management believes that, based on the information available to it, appropriate provisions have been made in respect of these matters at 31 December 2019 (see page 103). Where an individual provision is material, the fact that a provision has been made is stated and quantified, except to the extent doing so would be seriously prejudicial. Any provision recognised does not constitute an admission of wrongdoing or legal liability. It is not practicable to provide an aggregate estimate of potential liability for our legal proceedings and regulatory matters as a class of contingent liabilities.

Anti-money laundering and sanctions-related matters

In December 2012, among other agreements, HSBC Holdings plc ('HSBC Holdings') agreed to an undertaking with the UK Financial Service Authority, which was replaced by a Direction issued by the UK Financial Conduct Authority ('FCA') in 2013, and consented to a cease-and-desist order with the US Federal Reserve Board ('FRB'), both of which contained certain forward-looking anti-money laundering ('AML') and sanctions-related obligations. HSBC also agreed to retain an independent compliance monitor (who is, for FCA purposes, a 'Skilled Person' under section 166 of the Financial Services and Markets Act and, for FRB purposes, an 'Independent Consultant') to produce periodic assessments of the Group's AML and sanctions compliance programme (the 'Skilled Person/ Independent Consultant'). In December 2012, HSBC Holdings also entered into an agreement with the Office of Foreign Assets Control ('OFAC') regarding historical transactions involving parties subject to OFAC sanctions. Reflective of HSBC's significant progress in strengthening its financial crime risk management capabilities, HSBC's engagement with the current Skilled Person will be terminated and a new Skilled Person with a narrower mandate will be appointed to assess the remaining areas that require further work in order for HSBC to transition fully to business-as-usual financial crime risk management. The Independent Consultant will continue to carry out an annual OFAC compliance review at the FRB's discretion. The role of the Skilled Person/Independent Consultant is discussed on page 51.

Through the Skilled Person/Independent Consultant's prior reviews, as well as internal reviews conducted by HSBC Group, certain potential AML and sanctions compliance issues have been identified that HSBC Group is reviewing further with the FRB, FCA and/ or OFAC. The FCA is also conducting an investigation into HSBC Bank plc's and HSBC UK's compliance with UK money laundering regulations and financial crime systems and controls requirements. HSBC is cooperating with this investigation.

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

Foreign exchange related investigation

In January 2018, HSBC Holdings entered into a three-year deferred prosecution agreement with the Criminal Division of the US Department of Justice ('DoJ') (the 'FX DPA'), regarding fraudulent conduct in connection with two particular transactions in 2010 and 2011. This concluded the DoJ's investigation into HSBC's historical foreign exchange activities. Under the terms of the FX DPA, the HSBC Group has a number of ongoing obligations, including implementing enhancements to its internal controls and procedures in its Global Markets business, which will be the subject of annual reports to the DoJ.

In February 2019, various HSBC Group companies were named as defendants in a claim issued in the High Court of England and Wales that alleges foreign exchange-related misconduct. This matter is at an early stage. There are many factors that may affect the range of outcomes, and the resulting financial impact, of these matters, which could be significant.

Film finance litigation

In July and November 2015, two actions were brought by individuals against HSBC Private Bank (UK) Limited ('PBGB') in the High Court of England and Wales seeking damages on various alleged grounds, including breach of duty to the claimants, in connection with their participation in certain Ingenious film finance schemes. These actions are ongoing.

In December 2018, a separate action was brought against PBGB in the High Court of England and Wales by multiple claimants seeking damages for alleged unlawful means conspiracy and dishonest assistance in connection with lending provided by PBGB to third parties in respect of certain Ingenious film finance schemes in which the claimants participated. In June 2019, a similar claim was issued against PBGB in the High Court of England and Wales by additional claimants. These actions are ongoing.

In February 2019 and October 2019, PBGB received letters before claim by two largely separate groups of investors in Eclipse film finance schemes, each of which asserted various claims against PBGB in connection with its role in facilitating the design, promotion and operation of such schemes. These matters are at an early stage.

It is possible that additional actions or investigations will be initiated against PBGB as a result of its historical involvement in the provision of certain film finance related services.

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

Collections and recoveries related investigation

Various HSBC Group companies, including HSBC UK, are subject to an investigation by the FCA in connection with collections and recoveries operations in the UK. This matter is at a very early stage.

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

27 Related party transactions

The immediate parent company of the group is HSBC UK Holdings Limited and the ultimate parent company is HSBC Holdings plc. Both are incorporated in England.

Copies of these financial statements may be obtained from the following address:

HSBC Holdings plc
8 Canada Square
London E14 5HQ

The group's related parties include the parent, fellow subsidiaries, joint ventures, post-employment benefit plans for HSBC employees, Key Management Personnel ('KMP') of the bank and its ultimate parent company, HSBC Holdings plc, close family members of KMP and entities which are controlled, jointly controlled or significantly influenced by KMP or their close family members.

Particulars of transactions between the group and its related parties are tabulated below in accordance with IAS 24 'Related party disclosures'. The disclosure of the year-end balance and the highest amounts outstanding during the year are considered to be the most meaningful information to represent the amount of the transactions and outstanding balances during the year.

Key Management Personnel

The KMP of the bank are defined as those persons having authority and responsibility for planning, directing and controlling the activities of the bank and the group, and include the Directors of the bank, and directors and certain Group Managing Directors of HSBC Holdings plc. The emoluments of those KMP who are not directors of the bank are paid by other Group companies who make no recharge to the bank. It is not possible to make a reasonable apportionment of their emoluments in respect of the bank. Accordingly, no emoluments in respect of these KMP are included in the following disclosure.

The table below represents the compensation for Directors of the bank in exchange for services rendered to the bank for the period they served during the year.

Compensation of Key Management Personnel

	2019	2018[1]
	£000	£000
Short-term employee benefits	**5,703**	2,875
Other long-term employee benefits	**125**	120
Share-based payments	**578**	423
Year ended 31 Dec	**6,406**	3,418

1 *During the first six months of 2018 the banks' Executive Directors provided services to other companies within the HSBC Group and their services to the bank were incidental. Therefore the Executive Directors remuneration disclosed for 2018 represents the period from 1 July to 31 December 2018.*

Transactions and balances during the year with Key Management Personnel[1]

	2019		2018	
	Balance at 31 Dec[2]	**Highest amounts outstanding during year[3]**	Balance at 31 Dec[2]	Highest amounts outstanding during year[3]
	£m	**£m**	£m	£m
Advances and credits	**17**	**25**	11	12
Deposits	**17**	**83**	27	50

1 *Includes close family members and entities which are controlled or jointly controlled by KMP or their close family members.*
2 *Exchange rates applied for non-GBP amounts is as at 31 December 2019 and 2018.*
3 *Exchange rates applied for non-GBP amounts is the average for the year.*

The above transactions were made in the ordinary course of business and on substantially the same terms, including interest rates and security, as for comparable transactions with persons of a similar standing or, where applicable, with other employees. The transactions did not involve more than the normal risk of repayment or present other unfavourable features.

In addition to the requirements of IAS 24, particulars of advances (loans and quasi-loans), credits and guarantees entered into by the bank and its subsidiaries with Directors of the bank are required to be disclosed pursuant to section 413 of the Companies Act 2006. Under the Companies Act, there is no requirement to disclose transactions with other KMP.

Transactions with Directors: advances, credits and guarantees (Companies Act 2006)

	2019	2018
	Balance at 31 Dec £000	Balance at 31 Dec £000
Loans	**12,120**	5,361

Other related parties

Transactions and balances during the year with KMP of the bank's ultimate parent company[1,2]

	2019		2018	
	Balance at 31 Dec[3] £m	**Highest amounts outstanding during year[4] £m**	Balance at 31 Dec[3] £m	Highest amounts outstanding during year[4] £m
Advances and credits	**6**	**15**	12	12
Deposits	**–**	**–**	–	–

1 *Excludes those who are also KMP of the bank.*
2 *Includes close family members and entities which are controlled or jointly controlled by the KMP or their close family members.*
3 *Exchange rates applied for non-GBP amounts is as at 31 December 2019 and 2018.*
4 *Exchange rates applied for non-GBP amounts is the average for the year.*

The above transactions were made in the ordinary course of business and on substantially the same terms, including interest rates and security, as for comparable transactions with persons of a similar standing or, where applicable, with other employees. The transactions did not involve more than the normal risk of repayment or present other unfavourable features.

Transactions and balances during the year with the joint venture

	2019		2018	
	Balance at 31 Dec £m	**Highest balance during the year £m**	Balance at 31 Dec £m	Highest balance during the year £m
Unsubordinated amounts due from the joint venture	**83**	**90**	90	100
Amounts due to joint ventures	**21**	**21**	17	17
Guarantees and commitments	**300**	**480**	400	480

The group provides certain banking and financial services to its joint venture, including loans, overdrafts, interest and non-interest-bearing deposits and current accounts. Details of the interest in the joint venture are given in Note 12.

The group's transactions and balances during the year with HSBC Holdings plc and subsidiaries of HSBC Holdings plc

	2019				2018			
	Due to/from HSBC Holdings plc		**Due to/from subsidiaries of HSBC Holdings plc**		Due to/from HSBC Holdings plc		Due to/from subsidiaries of HSBC Holdings plc	
	31 Dec £m	**Highest balance £m**	**31 Dec £m**	**Highest balance £m**	31 Dec £m	Highest balance £m	31 Dec £m	Highest balance £m
Assets								
Derivatives	**–**	**–**	**45**	**46**	–	–	27	38
Loans and advances to banks	**–**	**–**	**671**	**1,526**	–	–	802	920
Loans and advances to customers	**–**	**–**	**–**	**–**	–	–	–	177
Other assets	**2**	**7**	**239**	**462**	8	8	416	1,842
Total related party assets at 31 Dec	**2**	**7**	**955**	**2,034**	8	8	1,245	2,977
Liabilities	**–**	**–**	**–**	**–**				
Deposits by banks	**–**	**–**	**283**	**1,293**	–	–	220	846
Customer accounts	**–**	**–**	**1**	**3**	–	784	1	61
Derivatives	**–**	**–**	**118**	**197**	–	–	211	224
Subordinated liabilities	**–**	**79**	**9,533**	**9,745**	79	79	4,858	4,859
Total related party liabilities at 31 Dec	**–**	**79**	**9,935**	**11,238**	79	863	5,290	5,990

	Due to/from HSBC Holdings plc		Due to/from subsidiaries of HSBC Holdings plc	
	2019	2018	**2019**	2018
	£m	£m	**£m**	£m
Income statement				
Interest income	**–**	–	**10**	(3)
Interest expense	**2**	4	**259**	59
Fee income	**–**	–	**64**	14
Fee expense	**–**	–	**43**	25
Other operating income	**–**	4	**16**	15
General and administrative expenses	**234**	74	**1,811**	894

The above outstanding balances arose in the ordinary course of business and on substantially the same terms, including interest rates and security, as for comparable transactions with third-party counterparties.

In 2018, all costs relating to the set-up of HSBC UK Bank plc up to the date of legal separation were incurred by HSBC Bank plc. These included directors' emoluments and auditors' remuneration.

The bank's transactions and balances during the year with HSBC UK Bank plc subsidiaries, HSBC Holdings plc and subsidiaries of HSBC Holdings plc

	2019						2018					
	Due to/from subsidiaries of HSBC UK Bank plc subsidiaries		**Due to/from HSBC Holdings plc**		**Due to/from subsidiaries of HSBC Holdings plc**		Due to/from subsidiaries of HSBC UK Bank plc subsidiaries		Due to/from HSBC Holdings plc		Due to/from subsidiaries of HSBC Holdings plc	
	31 Dec	**Highest balance**	**31 Dec**	**Highest balance**	**31 Dec**	**Highest balance**	31 Dec	Highest balance	31 Dec	Highest balance	31 Dec	Highest balance
	£m	**£m**	**£m**	**£m**	**£m**	**£m**	£m	£m	£m	£m	£m	£m
Assets												
Derivatives	**–**	**–**	**–**	**–**	**43**	**46**	–	–	–	–	24	37
Loans and advances to banks	**3,274**	**3,311**	**–**	**–**	**662**	**1,519**	2,729	2,729	–	–	706	913
Loans and advances to customers	**8,417**	**8,513**	**–**	**–**	**–**	**–**	8,005	8,005	–	–	–	–
Other assets	**1,895**	**2,303**	**1**	**6**	**226**	**455**	2,134	2,134	6	7	412	1,873
Total related party assets at 31 Dec	**13,586**	**14,127**	**1**	**6**	**931**	**2,020**	12,868	12,868	6	7	1,142	2,823
Liabilities												
Deposits by banks	**3,749**	**4,135**	**–**	**–**	**283**	**1,292**	3,238	3,385	–	–	220	846
Customer accounts	**373**	**373**	**–**	**–**	**1**	**1**	357	357	–	784	1	1
Derivatives	**–**	**–**	**–**	**–**	**117**	**192**	–	–	–	–	209	217
Subordinated liabilities	**–**	**–**	**–**	**–**	**9,454**	**9,666**	–	–	–	–	4,858	4,859
Total related party liabilities at 31 Dec	**4,122**	**4,508**	**–**	**–**	**9,855**	**11,151**	3,595	3,742	–	784	5,288	5,923

The above outstanding balances arose in the ordinary course of business and on substantially the same terms, including interest rates and security, as for comparable transactions with third-party counterparties.

Post-employment benefit plans

The group's pension funds had placed deposits of £169m (2018: £104m) with its banking subsidiaries, earning interest of £0.2m (2018: nil).

The above outstanding balances arose from the ordinary course of business and on substantially the same terms, including interest rates and security, as for comparable transactions with third-party counterparties.

28 Events after the balance sheet date

These accounts were approved by the Board of Directors on 17 February 2020 and authorised for issue.

On 13 February 2020, the Directors declared an interim dividend to ordinary shareholders of £100m in respect of the financial year ending 31 December 2019. No liability is recognised in the financial statements in respect of this dividend.

On 1 January 2020, substantially all of HSBC Private Bank (UK) Limited assets and liabilities were transferred to HSBC UK Bank plc. This was effected by way of a court sanctioned transfer scheme under Part VII of the Financial Services and Markets Act 2000. Further details are given in Note 13.

29 HSBC UK Bank plc's subsidiaries and joint ventures

In accordance with section 409 of the Companies Act 2006 a list of HSBC UK Bank plc subsidiaries and joint ventures, the registered office address and the effective percentage of equity owned at 31 December 2019 is disclosed below.

Unless otherwise stated, the share capital comprises ordinary or common shares which are held by HSBC UK Bank plc subsidiaries. The ownership percentage is provided for each undertaking. The undertakings below are consolidated by HSBC UK Bank plc unless otherwise indicated.

Subsidiaries

The undertakings below are consolidated by HSBC UK Bank plc.

Subsidiaries	% of share class held by immediate parent company (or by HSBC UK Bank plc where this varies)	Footnotes
Assetfinance December (F) Limited	100.00	4
Assetfinance June (D) Limited	100.00	4
Assetfinance March (D) Limited	100.00	4
Assetfinance September (G) Limited	100.00	4
B&Q Financial Services Limited	100.00	1, 5
Canada Square Nominees (UK) Limited	100.00	1, 6
HSBC Branch Nominee (UK) Limited	100.00	1,4
HSBC Client Share Offer Nominee (UK) Limited	100.00	1, 2, 7
HSBC Equipment Finance (UK) Limited	100.00	1, 4
HSBC Executor & Trustee Company (UK) Limited	100.00	4
HSBC Finance Limited	100.00	1, 6
HSBC Invoice Finance (UK) Limited	100.00	1, 8
HSBC Private Bank (UK) Limited	100.00	1, 6
HSBC Stockbrokers Nominee (UK) Limited	100.00	1, 2, 7
HSBC Trust Company (UK) Limited	100.00	1, 6
HSBC UK Client Nominee Limited	100.00	1, 4
HSBC Wealth Client Nominee Limited	100.00	1, 4
John Lewis Financial Services Limited	100.00	1, 6
Marks and Spencer Financial Services plc	100.00	1, 9
Marks and Spencer Unit Trust Management Limited	100.00	1, 9
Midland Bank (Branch Nominees) Limited	100.00	1, 4
Midland Nominees Limited	100.00	4
St Cross Trustees Limited	100.00	4
Turnsonic (Nominees) Limited	100.00	4

Joint ventures

The undertakings below are Joint Ventures and equity accounted.

Joint ventures	% of share class held by immediate parent company (or by HSBC UK Bank plc where this varies)	Footnotes
Vaultex UK Limited	50.00	3, 10

Footnotes

1	*Directly held by HSBC UK Bank plc*
2	*In Liquidation*
3	*Financial year ended 6 October 2019*

Registered Offices

4	*1 Centenary Square, Birmingham, United Kingdom, B1 1HQ*
5	*Camden House West, The Parade, Birmingham, United Kingdom, B1 3PY*
6	*8 Canada Square, London, United Kingdom, E14 5HQ*
7	*Hill House, 1 Little New Street, London, United Kingdom, EC4A 3TR*
8	*21 Farncombe Road, Worthing, United Kingdom, BN11 2BW*
9	*Kings Meadow Chester Business Park, Chester, United Kingdom, CH99 9FB*
10	*All Saints Triangle, Caledonian Road, London, United Kingdom, N1 9UT*

Reconciliation of Non-GAAP Financial Measures

Return on equity and return on tangible equity

Return on tangible equity ('RoTE') is computed by adjusting the reported equity for goodwill and intangibles. The adjustment to reported results and reported equity excludes amounts attributable to non-controlling interests. We provide RoTE in addition to return on equity ('RoE') as a way of assessing our performance, which is closely aligned to our capital position. The measures are calculated in USD in line with the standard HSBC Group wide calculation methodology.

The following table details the adjustments made to the reported results and equity:

Return on Equity and Return on Tangible Equity

	Year ended	
	31 Dec 2019	31 Dec 2018
	$m	$m
Profit		
Profit attributable to the ordinary shareholders of the parent company	**504**	923
Significant items (net of tax)	**1,544**	304
Other	**–**	(5)
Adjusted profit attributable to the ordinary shareholders of the parent company	**2,048**	1,222
Equity		
Average shareholders' equity	**28,567**	28,742
Additional Tier 1	**(2,813)**	(2,842)
Average ordinary shareholders' equity	**25,754**	25,900
Effect of goodwill and other intangibles (net of deferred tax)	**(5,013)**	(4,899)
Other	**–**	(23)
Average tangible ordinary shareholders' equity	**20,741**	20,978
Ratio	**%**	%
Return on equity (annualised)	**2.0**	6.4
Return on average tangible equity (annualised)	**2.4**	8.8
Adjusted return on average tangible equity (annualised)[1]	**9.9**	11.7

1 *In the event that the current IAS 19 Pension fund surplus was zero, additional CET1 capital would be required to be held and Adjusted RoTE would be 11.3% (2018: 13.7%); we refer to this as Pension Adjusted RoTE.*