HSBC HOLDINGS PLC
Form 20-F
March 08, 2011

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As filed with the Securities and Exchange Commission on March 8, 2011.

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 20-F

o **REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR 12(g) OF THE SECURITIES EXCHANGE ACT OF 1934**

Or

þ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended December 31, 2010

Or

o **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

Or

o **SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

Date of event requiring this shell company report ________

For the transition period from N/A to N/A
Commission file number: 1-14930
HSBC Holdings plc
(Exact name of Registrant as specified in its charter)

N/A	**United Kingdom**
(Translation of Registrant s name into English)	(Jurisdiction of incorporation or organisation)

8 Canada Square
London E14 5HQ
United Kingdom
(Address of principal executive offices)

Russell C Picot
8 Canada Square
London E14 5HQ
United Kingdom
Tel +44 (0) 20 7991 8888
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(Name, Telephone, Email and/or Facsimile number and Address of Company Contact Person)

Securities registered or to be registered pursuant to Section 12(b) of the Securities Exchange Act of 1934:

Title of each class	Name of each exchange on which registered
Ordinary Shares, nominal value US$0.50 each.	London Stock Exchange
	Hong Kong Stock Exchange
	Euronext Paris

	Bermuda Stock Exchange New York Stock Exchange*
American Depository Shares, each representing 5 Ordinary Shares of nominal value US$0.50 each.	New York Stock Exchange
6.20% Non-Cumulative Dollar Preference Shares, Series A	New York Stock Exchange*
American Depositary Shares, each representing one-fortieth of a Share of 6.20% Non-Cumulative Dollar Preference Shares, Series A	New York Stock Exchange
5.25% Subordinated Notes 2012	New York Stock Exchange
6.5% Subordinated Notes 2036	New York Stock Exchange
6.5% Subordinated Notes 2037	New York Stock Exchange
6.8% Subordinated Notes Due 2038	New York Stock Exchange
8.125% Perpetual Subordinated Capital Securities Exchangeable at the Issuer s Option into Non-Cumulative Dollar Preference Shares	New York Stock Exchange

Securities registered or to be registered pursuant to Section 12(g) of the Securities Exchange Act of 1934: None
Securities for which there is a reporting obligation pursuant to Section 15(d) of the Securities Exchange Act of 1934: None

Indicate the number of outstanding shares of each of the issuer s classes of capital or common stock as of the close of the period covered by the annual report:

Ordinary Shares, nominal value US$0.50 each 17,686,155,902

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

þ Yes o No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

o Yes þ No.

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

þ Yes o No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer þ	Accelerated filer o	Non-accelerated filer o (Do not check if a smaller reporting company)

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP o	International Financial Reporting Standards as issued by the International Accounting Standards Board þ	Other o

If Other has been checked in response to the previous question indicate by check mark which financial statement item the registrant has elected to follow.

o Item 17 o Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

o Yes þ No

* Not for trading, but only in connection with the registration of American Depositary Shares.

HSBC HOLDINGS PLC
Annual Report and Accounts 2010

Certain defined terms
Unless the context requires otherwise, HSBC Holdings means HSBC Holdings plc and HSBC , the Group , we , us and our refers to HSBC Holdings together with its subsidiaries. Within this document the Hong Kong Special Administrative Region of the People s Republic of China is referred to as Hong Kong . When used in the terms shareholders equity and total shareholders equity , shareholders means holders of HSBC Holdings ordinary shares and those preference shares classified as equity. The abbreviations US$m and US$bn represent millions and billions (thousands of millions) of US dollars, respectively.
Financial statements
The consolidated financial statements of HSBC and the separate financial statements of HSBC Holdings have been prepared in accordance with International Financial Reporting Standards (IFRSs) as issued by the International Accounting Standards Board (IASB) and as endorsed by the European Union (EU). EU-endorsed IFRSs may differ from IFRSs as issued by the IASB if, at any point in time, new or amended IFRSs have not been endorsed by the EU. At 31 December 2010, there were no unendorsed standards effective for the year ended 31 December 2010 affecting these consolidated and separate financial statements, and there was no difference between IFRSs endorsed by the EU and IFRSs issued by the IASB in terms of their application to HSBC. Accordingly, HSBC s financial statements for the year ended 31 December 2010 are prepared in accordance with IFRSs as issued by the IASB.

We use the US dollar as our presentation currency because the US dollar and currencies linked to it form the major currency bloc in which we transact and fund our business. Unless otherwise stated, the information presented in this document has been prepared in accordance with IFRSs.

When reference to underlying or underlying basis is made in tables or commentaries, comparative information has been expressed at constant currency (see page 14), eliminating the impact of fair value movements in respect of credit spread changes on HSBC s own debt and adjusting for the effects of acquisitions and disposals. A reconciliation of reported and underlying profit before tax is presented on page 15.
Report of the Directors
The information set out in the Report of the Directors on pages 2 to 219 does not constitute the directors report included in the Company s Annual Report and Accounts for the year ended 31 December 2010 under Section 415 of the Companies Act 2006 as it includes certain supplementary information and explanations.
Contents

1 *Detailed contents are provided on the referenced pages.*

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HSBC HOLDINGS PLC

Report of the Directors: Overview

Overview

Headquartered in London, HSBC is one of the world s largest banking and financial services organisations and one of the industry s most valuable brands. We provide a comprehensive range of financial services to around 95 million customers through two customer groups, Personal Financial Services (including consumer finance), and Commercial Banking, and two global businesses, Global Banking and Markets, and Global Private Banking.

Our international network covers 87 countries and territories in six geographical regions; Europe, Hong Kong, Rest of Asia-Pacific, the Middle East, North America and Latin America.

With listings on the London, Hong Kong, New York, Paris and Bermuda stock exchanges, shares in HSBC Holdings plc are held by over 221,000 shareholders in 127 countries and territories.

Highlights

Pre-tax profit more than doubled to US$19bn on a reported basis.

Underlying pre-tax profit up by almost US$5bn or 36% to US$18.4bn.

Profitable in every customer group and region, including North America, for the first time since 2006.

Dividends declared in respect of 2010 totalled US$6.3bn, or US$0.36 per ordinary share, with a fourth interim dividend for 2010 of US$0.12 per ordinary share.

Continued capital generation core tier 1 ratio increased to 10.5% from 9.4%.

Customer lending up 8% to US$958bn; deposits up 7% to US$1.2 trillion on an underlying basis.

Cover theme

An evening view of the Central Elevated Walkway in Hong Kong s business district. Used by tens of thousands of commuters every day, this walkway forms a vital artery through the heart of Asia s pre-eminent financial centre, which hosts over 190 banks and deposit-taking companies from all over the world.

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Report of the Directors: Overview (continued)

Financial highlights

For the year

Profit before taxation	**Underlying profit before taxation**	**Total operating income**
US$19,037m *up 169%*	US$18,366m *up 36%*	US$80,014m *up 2%*
2009: US$7,079m 2008: US$9,307m	2009: US$13,482m	2009: US$78,631m 2008: US$88,571m

Net operating income before loan impairment charges and other credit risk provisions	**Profit attributable to shareholders of the parent company**
US$68,247m *up 3%*	US$13,159m *up 126%*
2009: US$66,181m 2008: US$81,682m	2009: US$5,834m 2008: US$5,728m

Earnings per share and dividends per share

Earnings per share	**Dividends per share[1]**
US$0.73 *up 115%*	US$0.34
2009: US$0.34 2008: US$0.41	2009: US$0.34 2008: US$0.93

At the year-end

Loans and advances to customers	**Customer accounts**	**Ratio of customer advances to customer accounts**
US$958bn *up 7%*	US$1,228bn *up 6%*	78.1%
2009: US$896bn	2009: US$1,159bn	2009: 77.3%

2008: US$933bn	2008: US$1,115bn	2008: 83.6%
Total equity	**Average total shareholders equity to average total assets**	**Risk-weighted assets**
US$155bn *up 14%*	5.5%	US$1,103bn *down 3%*
2009: US$136bn 2008: US$100bn	2009: 4.7% 2008: 4.9%	2009: US$1,133bn 2008: US$1,148bn

Capital ratios

Core tier 1 ratio	**Tier 1 ratio**	**Total capital ratio**
10.5%	12.1%	15.2%
2009: 9.4% 2008: 7.0%	2009: 10.8% 2008: 8.3%	2009: 13.7% 2008: 11.4%

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HSBC HOLDINGS PLC
Report of the Directors: Overview (continued)

Performance ratios

Credit coverage ratios

Loan impairment charges to total operating income	**Loan impairment charges to average gross customer advances**	**Total impairment allowances to impaired loans at year-end**
16.9%	1.5%	71.6%
2009: 31.7% 2008: 27.2%	2009: 2.8% 2008: 2.5%	2009: 83.2% 2008: 94.3%

Return ratios

Return on average invested capital[2]	**Return on average shareholders equity**[3]	**Post-tax return on average total assets**	**Post-tax return on average risk-weighted assets**
8.7%	9.5%	0.6%	1.3%
2009: 4.1% 2008: 4.0%	2009: 5.1% 2008: 4.7%	2009: 0.3% 2008: 0.3%	2009: 0.6% 2008: 0.6%

Efficiency and revenue mix ratios

Cost efficiency ratio[4]	**Net interest income to total operating income**	**Net fee income to total operating income**	**Net trading income to total operating income**
55.2%	49.3%	21.7%	9.0%
2009: 52.0% 2008: 60.1%	2009: 51.8% 2008: 48.1%	2009: 22.5% 2008: 22.6%	2009: 12.5% 2008: 7.4%

Share information at the year-end

			Closing market price	
US$0.50 ordinary shares in issue	**Market capitalisation**	London	Hong Kong	American Depositary Share[5]

17,686m	US$180bn	£6.51	HK$79.70	US$51.04
2009: 17,408m	2009: US$199bn	2009: £7.09	2009: HK$89.40	2009: US$57.09
2008: 12,105m	2008: US$114bn	2008: £5.77	2008: HK$67.81	2008: US$44.15

	Total shareholder return[6]		
	Over 1 year	Over 3 years	Over 5 years
To 31 December 2010	95.3	103.4	103.4
Benchmarks:			
FTSE 100[7]	112.6	102.8	126.3
MSCI World[7]	115.9	111.0	127.0
MSCI Banks[7]	103.7	81.9	79.0

For footnotes, see page 83.

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HSBC HOLDINGS PLC
Report of the Directors: Overview (continued)

Cautionary statement regarding forward-looking statements

The *Annual Report and Accounts 2010* contains certain forward-looking statements with respect to HSBC s financial condition, results of operations and business.

Statements that are not historical facts, including statements about HSBC s beliefs and expectations, are forward-looking statements. Words such as expects , anticipates , intends , plans , believes , seeks , estimates , 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, and it should not be assumed that they have been revised or updated in the light of new information or future events.

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

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

changes in general economic conditions in the markets in which we operate, such as continuing or deepening recessions and fluctuations in employment beyond those factored into consensus forecasts; changes in foreign exchange rates and interest rates; volatility in equity markets; lack of liquidity in wholesale funding markets; illiquidity and downward price pressure in national real estate markets; adverse changes in central banks policies with respect to the provision of liquidity support to financial markets; heightened market concerns over sovereign creditworthiness in over-indebted countries; adverse changes in the funding status of public or private defined benefit pensions; and consumer perception as to the continuing availability of credit and price competition in the market segments we serve;

changes in government policy and regulation, including the monetary, interest rate and other policies of central banks and other regulatory authorities; initiatives to change the size, scope of activities and interconnectedness of financial institutions in connection with the implementation of stricter regulation of financial institutions in key markets worldwide; revised capital and liquidity benchmarks which could serve to deleverage bank balance sheets and lower returns available from the current business model and portfolio mix; imposition of levies or taxes designed to change business mix and risk appetite; the practices, pricing or responsibilities of financial institutions serving their consumer markets; expropriation, nationalisation, confiscation of assets and changes in legislation relating to foreign ownership; changes in bankruptcy legislation in the principal markets in which we operate and the consequences thereof; general changes in government policy that may significantly influence investor decisions; extraordinary government actions as a result of current market turmoil; other unfavourable political or diplomatic developments producing social instability or legal uncertainty which in turn may affect demand for our products and services; the costs, effects and outcomes of product regulatory reviews, actions or litigation, including any additional compliance requirements; and the effects of competition in the markets where we operate including increased competition from non-bank financial services companies, including securities firms; and factors specific to HSBC, including our success in adequately identifying the risks we face, such as the incidence of loan losses or delinquency, and managing those risks (through account management, hedging and other techniques). Effective risk management depends on, among other things, our ability through stress testing and other techniques to prepare for events that cannot be captured by the statistical models it uses; and our success in addressing operational, legal and regulatory, and litigation challenges.

3(a)

HSBC HOLDINGS PLC
Report of the Directors: Overview (continued)

Group Chairman s Statement

When I took on the role of Chairman less than 90 days ago, I was acutely aware of the challenges facing our industry. I was conscious too of the need to demonstrate to all of our stakeholders that HSBC understands the responsibilities that accompany the systemic significance which continued success has built for HSBC in many of the markets in which we operate, not least those in Asia, given their historical significance to the Group. 145 years after we were founded, Hong Kong and the rest of Asia remain at the heart of HSBC s strength and identity and our commitment to the region is unwavering.

I fully acknowledge that our scale, the trust that our depositors place in us and our relevance to our personal and corporate clients for their financing, banking, investment and risk management needs all depend upon our maintaining our reputation and our integrity.

I also understand how important it is for you, our shareholders, that HSBC builds sustainable long-term value that is reflected through the share price and rebuilds, as quickly as competing regulatory demands allow, the dividend that was reduced during the financial crisis.

I firmly believe that HSBC has the people, the financial strength and the organisational structure best able to deliver all of the above and it is a privilege to have the opportunity to serve as Group Chairman as we enter a fresh chapter in our history.

Before I go any further, I want to pay tribute to both Stephen Green and Michael Geoghegan, who stepped down at the end of last year from their roles as Group Chairman and Group Chief Executive after, respectively, 28 and 37 years service to HSBC. It fell to them to be at the helm as HSBC navigated its way through the worst financial crisis since the 1930s. Mike led from the front in addressing the problems in our consumer finance subsidiary in the United States and in reshaping HSBC s organisational structure and operational practices in order to better and more efficiently serve an increasingly interconnected world. Stephen s personal reputation for integrity and probity stood out and distinguished HSBC during a period of intense disaffection with the banking industry. For their contribution over many years we owe them a deep debt of gratitude and wish them both well.

Our performance in 2010

The Group Chief Executive s Business Review sets out clearly how HSBC delivered a much improved balance of profits in 2010. It is reassuring to see our Personal Financial Services businesses returning to profitability in aggregate and Commercial Banking growing significantly, largely in emerging markets. These achievements augmented another year of strong performance in Global Banking and Markets.

Earnings per share improved strongly, rising by 115% to reach US$0.73 per share.

The Group s capital position also strengthened with the core tier 1 ratio, the ratio most favoured by regulators as it comprises equity capital after regulatory adjustments and deductions, increasing from 9.4% to 10.5%, largely due to profit retention throughout the year.

As a consequence of this strong capital generation, together with greater clarity on the direction of regulatory reform of capital requirements and an improving economic backdrop in the developed world particularly in the United States the Board has approved increases in both the final dividend payment in respect of 2010 and the planned quarterly dividends for 2011. The final dividend for 2010, payable on 5 May 2011 to shareholders on the register on 17 March 2011, will be 12 cents per ordinary share, up from 10 cents at the same point last year. For the remainder of 2011 we plan to pay quarterly dividends of nine cents for each of the first three quarters compared with eight cents in respect of the equivalent quarters of 2010.

A new leadership team

We enter 2011 with a new leadership team, but only in the sense of changed roles. Everyone has worked together over many years and there is immense experience to draw on both from within HSBC and from earlier careers at peer organisations. Stuart Gulliver is leading the management team as Group Chief Executive. His clear objective is to deliver sustainable long-term value for shareholders consistently in a manner that maintains the confidence of all other key stakeholders in our businesses including depositors, counterparties, long-term creditors, customers, employees, regulators and governments. His review on pages 7 to 9 gives an insight into his immediate priorities.

Everything we do is governed by the imperative of upholding HSBC s corporate reputation and character at the highest level and adding further strength to our brand; we deeply regret that a number of weaknesses in regulatory compliance were highlighted in 2010 and we are resolved to remedy these and reinforce the high standards we demand of ourselves.

For my part, I shall be focusing on engaging at the highest level in the regulatory reform debates that will, in large part, shape our future. I shall also lead the Board in the stewardship and review of performance of our financial and human resources.

In the interest of full transparency, we have today published on our website the respective roles and responsibilities of the Group Chairman, the Deputy Chairman and Senior Independent Director and the Group Chief Executive.

Board changes

I have already paid tribute to the contributions of Stephen Green and Michael Geoghegan. Vincent Cheng has indicated that he will step down at the next AGM and on behalf of the Board I want to thank him for his immense contribution in many roles over 33 years. Vincent will retain an association with the Group by taking on an advisory role to the Group Chief Executive on regional matters. Laura Cha will join the Board on 1 March; Laura has been Deputy Chair of The Hongkong and Shanghai Banking Corporation Limited for four years and brings a wealth of experience of China; fuller details of her background and experience are set out in the Directors Report.

Regulatory update

There was much progress made during 2010 on the regulatory reform agenda. Although there is still a great deal to do, the shape of capital requirements was broadly clarified and an implementation timetable stretching out to 2019 was agreed to allow time for the industry to adjust progressively. A minimum common equity tier 1 ratio of 7%, including a capital conservation buffer, has been agreed. HSBC already meets this threshold requirement. The Group Chief Executive s Business Review addresses how these revised requirements will impact our targeted return on equity.

During 2011, the debate will be dominated by consideration of the calibration of minimum liquidity standards. Although it is clear that liquidity and funding weaknesses were key elements contributing to the crisis, HSBC agrees with the industry consensus that the revised requirements in these areas are overly conservative and could lead to unnecessary deleveraging at a time of fragile economic recovery in much of the developed world. It will be a near impossibility for the industry to expand business lending at the same time as increasing the amount of deposits deployed in government bonds while, for many banks but not HSBC, reducing dependency on central bank liquidity support arrangements. It is to be hoped that the observation period, which starts this year and precedes the formal introduction of the new requirements, will inform a recalibration of these minimum liquidity standards.

A second debate of importance to HSBC s shareholders in 2011 will concern the designation of Systemically Important Financial Institutions (SIFI s). Consideration is being given in the regulatory community to mandating higher capital requirements, together with more intense supervision, for institutions classified as SIFIs. We agree with heightened supervision but it is not clear that the reduced shareholder returns that would follow the imposition of incremental capital would be compensated for by improved stability. Classification as a SIFI with a requirement to hold incremental capital would, however, probably lead others to favour SIFIs as counterparties, and may therefore have the unintended consequence of further concentrating the industry.

HSBC s position is that systemic importance should not be determined by size alone. It is clear, however, that, on almost any basis, HSBC would be classified as systemically important. For this reason we are engaging fully in the debate around the consequences of designation as a SIFI. In particular, we draw attention to the benefits of our corporate organisation through separate subsidiaries in mitigation against the imposition of incremental capital for SIFIs based on size alone.

In October 2010, the UK government confirmed its intention to raise the sum of £2.5bn (US$3.9bn) through a levy on bank balance sheets, and recently announced it will accelerate the full impact of this levy to 2011. We take no issue with the right of the UK government to raise a levy on the banking industry, particularly when having had to risk taxpayers   money to rescue a number of important UK institutions. However, as the proposed levy is to

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Report of the Directors: Overview (continued)

be applied to the consolidated balance sheet, it applies beyond the legal boundary of the domestic institution to include overseas operations conducted through separately capitalised subsidiaries. This therefore constitutes an additional cost of basing a growing multinational banking group in the UK.

We intend to clarify in each set of results going forward the impact of the levy, split between UK and overseas operations, and Stuart Gulliver covers this in more detail in his review. We regard the levy, which is not tax deductible, as akin to a distribution of profits. For this reason, we intend to add to future shareholder dividends that would otherwise be paid, any amount saved in the event that the levy is restructured or relieved in due course.

The role of banks in society

The recent crisis has caused a proper introspection as to the role that banks play in society and at HSBC we welcome this. Banking is not simply about money. It is about helping individuals and organisations within society to meet personal and corporate objectives by facilitating access to financial capital and protecting value for those who make capital available. Payment mechanisms, the provision of long-term credit, trade finance, hedging and other risk management products, deposit, investment and retirement services are but a few of the activities through which banking groups contribute to today s financial system. Society cannot function without an effective financial system that delivers value to those it serves at an intermediation cost that is proportionate to the value created. Somehow, many participants and not just banks, lost sight of this basic principle in the run-up to the recent financial crisis and the consequences for all have, inevitably, been far reaching. There is no doubt that the scale of regulatory reform will bring many challenges, but it will also open new opportunities.

At HSBC, we shall not forget what happened to precipitate the scale of reform now underway. Although the financial turmoil arising from the events of 2007-2008 has largely moderated, in large part as a result of co-ordinated government action and support to the financial system, we enter 2011 with humility, ready to apply right across HSBC all of the lessons learned, notwithstanding that HSBC itself neither sought nor received support from any government.

Society has a right to ask if banks get it . At HSBC, we do and we are focused on embedding the necessary changes in our business model for long-term sustainable value creation. But we also do not forget that value creation depends upon HSBC recruiting, training and retaining the right talent in order to manage the risks we accept through intermediating customer flows; design solutions to address complex financial problems; build enduring relationships with core customers; build confidence in the Group s financial strength; and create the strategic options that offer the next generation fresh opportunities to continue building sustainable value.

In this globalised world, there is intense competition for the best people and, given our long history within and connections into the faster-growing developing markets, our best people are highly marketable. It would be irresponsible to allow our comparative advantages to wither by ignoring the market forces that exist around compensation, even though we understand how sensitive this subject is. Reform in this area can only be achieved if there is concerted international agreement on limiting the quantum of pay as well as harmonising pay structures but there appears to be no appetite to take the initiative on this. Our duty to shareholders is to build sustainable value in the economic and competitive environment in which we operate and our principal resource for achieving this is human talent. Under the governance of the Board, we will continue to operate and apply remuneration policies and practices that take full recognition of best practice and are aligned with the long-term interests of shareholders.

HSBC s people

Finally, I want to pay tribute to my 307,000 colleagues. So many of HSBC s people have exemplified commitment and endeavour again in 2010, helping our customers and clients to meet their financial objectives while taking on the additional burden of preparing for regulatory change. This has been done against a backdrop of continuing broad-based fiscal support to many economies, with public opinion consistently and highly critical of our industry. As

I look forward, it is the combination of the capabilities of HSBC s people, their determination to do the right thing for our customers and their deep sense of responsibility to the communities they serve that makes me confident that HSBC will play a leading role in rebuilding the trust that our industry has lost and, by doing so, will build sustainable value for you, our shareholders.

D J Flint, *Group Chairman*
28 February 2011

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HSBC HOLDINGS PLC
Report of the Directors: Overview (continued)

Group Chief Executive s Business Review

Underlying financial performance continued to improve in 2010 and shareholders continued to benefit from HSBC s universal banking model. All regions and customer groups were profitable, as Personal Financial Services and North America returned to profit. Commercial Banking made an increased contribution to underlying earnings and Global Banking and Markets also remained strongly profitable, albeit behind 2009 s record performance, reflecting a well-balanced and diversified business.

Credit experience continued to improve, as a result of a stronger global economy and our actions to reduce balance sheet risk. As a globally-connected bank with a growing presence across the world s faster-growing regions, HSBC also benefited from higher trade volumes and strong momentum in emerging economies, especially in Asia. Asia contributed the largest proportion to underlying pre-tax profits, while the contributions made by Latin America and the Middle East also increased. Together with our conservative management of the balance sheet, this improved performance allowed us to concentrate on serving our customers and to further strengthen our capital position.

Group performance headlines[1]

Profit before tax improved year on year. On a reported basis, profits increased by nearly US$12bn from US$7.1bn to US$19bn. On an underlying basis, profits increased by 36%, or almost US$5bn, from US$13.5bn to US$18.4bn.

1 *All figures are discussed on a reported basis and all references to profits are profits before tax unless otherwise stated.*

In a period of sustained low interest rates, revenues remained constrained, reflecting four principal factors: reducing loan balances in our US business; lower trading income in Global Banking and Markets resulting from lower client activity; adverse fair value movements on non-qualifying hedges; and a reduced contribution from Balance Sheet Management in line with earlier guidance.

Strong asset growth in Commercial Banking, particularly in Asia, higher trade-related revenues generally, and expansion of our wealth management business, again most notably in Asia, partially offset these revenue pressures.

Loan impairment charges reduced by almost half to US$14.0bn. All regions and customer groups improved. The US experienced the greatest improvement, largely in the cards and consumer finance portfolios. Loan impairment charges also declined significantly in Latin America and the Middle East.

In Global Banking and Markets, loan impairment charges fell significantly, notably in Europe as economic conditions improved. Credit risk provisions reduced by US$1bn to US$0.4bn in the available-for-sale asset-backed-securities portfolios due to a slowing in the rate of anticipated losses on underlying assets, in line with previous guidance. The associated available for sale reserve declined to US$6.4bn from US$12.2bn.

The cost efficiency ratio rose to 55.2%, which is above our target range and unacceptable to me. The causes were constrained revenues and, in part, investment in strategic growth initiatives across the business together with higher staff costs. It additionally reflected one-off payroll taxes of US$0.3bn paid in 2010 in respect of the previous year and a pension accounting credit of US$0.5bn in 2009 and US$0.1bn in 2010. However, it is also clear that we need to re-engineer the business to remove inefficiencies.

Return on average total shareholders equity rose from 5.1% to 9.5%, reflecting increased profit generation during the year.

HSBC continued to grow its capital base and strengthen its capital ratios further. The core tier 1 ratio increased from 9.4% to 10.5%, as a result of capital generation and lower risk weighted assets.

Total loans and advances to customers increased by 7% to US$958bn while deposits rose by 6% to US$1.2 trillion.

Impact of the evolving regulatory environment on the business

Much of the detail around the potential impact of change for banks remains uncertain. However, analysis of what we know confirms that our ability to generate capital and manage our risk-weighted assets positions HSBC strongly and competitively within the industry as the pace of change intensifies.

HSBC fully supports the rationale of the Basel III proposals which require banks to hold more capital. This is absolutely core to ensuring that governments and taxpayers are better protected in future than they have been in the past.

Certain aspects of the Basel III rules remain uncertain as to interpretation and application by national regulators. Notably, this includes any capital requirements which may be imposed on the Group over the implementation period in respect of the countercyclical capital buffer and any additional regulatory requirements for SIFIs. However, we believe that ultimately the level for the common equity tier 1 ratio of the Group may lie in the range 9.5 to 10.5%. This exceeds the minimum requirement for common equity tier 1 capital plus the capital conservation buffer.

We have estimated the pro forma common equity tier 1 ratio of the Group based on our interpretation of the new Basel III rules as they will apply from 1 January 2019, based on the position of the Group at year-end 2010. The rules will be phased in from 2013 with a gradual impact and we have estimated that their full application, on a proforma basis, would result in a common equity tier 1 ratio which is lower than the Basel II core tier 1 ratio by some 250 300 basis points. The changes relate to increased capital deductions, new regulatory adjustments and increases in risk-weighted assets. However, as the changes will progressively take effect over six years leading up to 2019 and as HSBC has a strong track record of capital generation and actively manages its risk-weighted assets, we are confident in our ability to mitigate the effect of the new rules before they come into force.

Last year, HSBC committed to reviewing its target shareholder return on equity once the effects of new regulation became clearer. Now that we have better visibility on the impact of increased capital requirements, we believe that higher costs of the evolving regulatory framework will, all other things being equal, depress returns for shareholders of banks. We will therefore target a return on average shareholders equity of 12-15% in the future.

As Group Chief Executive, it is right that, in managing the business and developing Group strategy, my principal office should be in Hong Kong a global financial hub of growing importance at the centre of HSBC s strategically most important region. However, the company is headquartered in London and we hope to remain there. London s pre-eminence as an international financial services centre is widely recognised and well-deserved and reflects successful government policy over decades to build that position. It is therefore important to us that the UK s competitive position is protected and sustained. Appropriate supervision is an important part of the larger equation. Policymakers should continue to legislate and regulate, but they must not destroy London s competitive position in the process.

As the Group Chairman has outlined, new legislation is expected to be enacted in the UK, effective from the start of 2011, one curious consequence of which is an explicit incremental cost of being headquartered in the UK for any global bank. Had this been applied for 2010, this annual charge would have amounted to approximately US$0.6bn in HSBC s case. Moreover, the overseas balance sheet would account for the majority of the annual charge, with the UK balance sheet accounting for approximately one third of the total.

Outlook

We have been closely watching events unfold in parts of the Middle East and North Africa. Our primary concern is for the security of our 12,000 staff across the region and we continue to work to ensure their safety. We have also activated robust continuity plans so that we can also stay open for business and support the needs of our customers. As a strongly capitalised global bank, HSBC s financial performance has not been materially affected by events to date. HSBC has been present in the Middle East for more than 50 years and we remain absolutely committed to its future. We also believe that the region s economies have a number of structural strengths which leave us positive on the longer-term outlook.

In the short term, risks to global growth remain, not least from an elevated oil price. We therefore expect cyclical volatility to continue including in emerging markets and progress is unlikely to be linear. In the longer term, we believe that growth

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HSBC HOLDINGS PLC
Report of the Directors: Overview (continued)

rates in many Western markets will continue to significantly underperform those of the emerging world. Emerging markets are no longer simply leading the recovery from a Western crisis; the growth gap has become a sustained secular trend.

The global economy s structural position also requires fundamental readjustment. Many Western economies must still deal with a large overhang of household and government debt and weak growth and high unemployment will make this a slow and painful process. As faster-growing nations seek to limit the effect of Western monetary policy on their own economies, we cannot discount the risk of increased tension over exchange rate and trade issues.

HSBC s balance sheet remains strongly positioned to benefit from future interest rate rises. We are realistic that, in many developed countries at least, historically low rates may continue to constrain income growth in the near-term. Nevertheless, maintaining a conservative liquidity position is core to our proposition and to our funding strength. In our risk appetite statement approved by the Board we have set a maximum advances-to-deposits ratio for the Group of 90%. This underlines our continuing commitment to a high level of liquidity and reflects our philosophy that HSBC should not be reliant on wholesale markets for funding. Even with a ratio currently slightly below 80%, we have capacity for further lending growth.

In the short-term, we expect the benefits of asset growth achieved in 2010 to continue to flow into revenues. In the medium-term, we will continue to target growth in the most strategically attractive markets for HSBC and build our capabilities in connectivity, one of our distinctive strengths as a globally-connected bank.

At the same time, with demand in many developed markets constrained and interest spreads remaining compressed, we fully recognise the importance of ever more robust cost management discipline and the need to continue re-engineering the business to improve efficiency.

Furthermore, capital is becoming a scarcer resource and, as a new regulatory environment evolves, I am committed to making capital allocation a more disciplined and rigorous process at HSBC in order to drive the correct investment decisions for the future.

We will talk more to investors about each of these initiatives later in the spring. However, as a result of this focus, we are committed to delivering a cost efficiency ratio and a return on average shareholders equity within our published target range.

We also recognise the importance of reliable dividend income for our shareholders and I believe it should be possible to benchmark a payout ratio of between 40-60% of attributable profits under normal market conditions.

In closing, I would like to acknowledge the huge contribution that my predecessor, Mike Geoghegan, made to HSBC in his five years as Group Chief Executive not least during 2010 and I wish him well for the future.

Finally, I am pleased to report that we have had a good start to the year, with continued momentum in lending, mainly in emerging markets and in respect of global trade.

S T Gulliver, *Group Chief Executive*
28 February 2011

HSBC HOLDINGS PLC
Report of the Directors: Overview (continued)

Principal activities

HSBC is one of the largest banking and financial services organisations in the world, with a market capitalisation of US$180bn at 31 December 2010. We are headquartered in London.

As The world s local bank , we combine the largest global emerging markets banking business and a uniquely cosmopolitan customer base with an extensive international network and substantial financial strength.

HSBC operates through long-established businesses and has an international network of some 7,500 offices in 87 countries and territories in six geographical regions; Europe, Hong Kong, Rest of Asia-Pacific, the Middle East, North America and Latin America.

Our products and services are delivered through two customer groups, Personal Financial Services (PFS) and Commercial Banking (CMB), and two global businesses, Global Banking and Markets (GB&M), and Global Private Banking (GPB). PFS incorporates the Group s consumer finance businesses, the largest of which is HSBC Finance Corporation (HSBC Finance).

Taken together, our five largest customers do not account for more than 1% of our income.

We have contractual and other arrangements with numerous third parties in support of our business activities. None of the arrangements is individually considered to be essential to the business of the Group.

There were no significant acquisitions during the year (for details of acquisitions see page 340).

Strategic direction

Our objective is to deliver sustainable long-term value to shareholders through consistent earnings and superior risk-adjusted returns.

Our strategy is to be the world s leading international bank, by:

- leveraging the HSBC brand and our network of businesses which covers the world s most relevant geographies. This network provides access to the world s fastest growing economies, for example Greater China. We serve companies as they grow and become more international and individuals as they become wealthier and require more sophisticated financial services, such as wealth management; and

- competing as a universal bank across the full financial services spectrum only where we have scale and can achieve appropriate returns. This implies building scale in attractive geographical regions and businesses where we can be competitive and reviewing businesses which do not meet our financial hurdles.

The strategy reflects the key trends which are shaping the global economy. In particular, we recognise that over the long term, developing markets are growing faster than mature economies and connectivity continues to increase as world trade is expanding at a greater rate than gross domestic product, generating increased demand for financial services. We are, therefore, continuing to direct incremental investment primarily to the faster growing markets and client segments which have international connectivity. In order to deliver this strategy we pursue a series of initiatives, reflected in the Group s key performance indicators:

- enhance efficiency by taking full advantage of local, regional and global economies of scale, in particular by adopting a common systems architecture wherever possible;

- maintain capital strength and a strong liquidity position. Capital and liquidity are critical for our strategy and are the foundation of decisions about the pace and direction of investment; and

- align objectives and incentives to motivate and reward staff for being fully engaged in delivering the strategy.

HSBC HOLDINGS PLC
Report of the Directors: Overview (continued)

Top and emerging risks

All of our activities involve, to varying degrees, the measurement, evaluation, acceptance and management of risk or combinations of risks. We classify risks as top and emerging . A top risk is a current, visible risk with the potential to have a material effect on our financial results or our reputation. An emerging risk is one which has large unknown components which could have a material impact on our long-term strategy. Top and emerging risks are viewed as falling under the following four broad categories:

- challenges to our business operations;
- challenges to our governance and internal control systems;
- macro-economic and geopolitical risk; and
- macro-prudential and regulatory risks to our business model.

The top and emerging risks are summarised below:

Challenges to our business operations

- Challenges to our operating model in an economic downturn (in developed countries) and rapid growth (in emerging markets)
- Internet crime and fraud

Challenges to our governance and internal control systems

- Level of change creating operational complexity
- Information security risk

Macro-economic and geopolitical risk

- Potential emerging markets asset bubble
- Increased geopolitical risk in Asia-Pacific and Middle East regions

Macro-prudential and regulatory risks to our business model

- Regulatory change impacting our business model and Group profitability
- Regulatory requirements affecting conduct of business

Key performance indicators

The Board of Directors and the Group Management Board (GMB) monitor HSBC s progress against its strategic objectives. Progress is assessed by comparison with our strategy, our operating plan targets and our historical performance using both financial and non-financial measures.

Following a review of our high-level key performance indicators (KPI s), the GMB decided to make the following changes to the Group s published indicators in order to restrict their number to those which most accurately reflect its management priorities. The Group now has seven financial and three non-financial KPIs.

the ratio of advances to core funding has been added to highlight the relationship between loans and advances to customers and core customer deposits in our principal banking entities;

tier 1 capital has been added as a primary indicator of the strength of our capital base, and its ability to support the growth of the business and meet regulatory capital requirements;

revenue growth, revenue mix factors and credit performance as measured by risk-adjusted margin have been replaced with risk-adjusted revenue growth;

the GMB will prioritise return on average total shareholders equity in place of return on average invested capital, which has therefore been excluded; and

customer transactions processed and percentage of information technology (IT) services meeting targets form part of management information within our IT function. However, the GMB decided that these measures, which we have previously disclosed, were not appropriate proxies for assessing efficiencies and progress with implementing standard systems architecture.

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Report of the Directors: Overview (continued)

Strategic objectives	Deliver consistent earnings and superior risk-adjusted returns		
	Risk-adjusted revenue growth (2010: underlying growth 15%)	**Basic earnings per ordinary share**	**Dividends per share growth**
Key Performance Indicators	**Measure**: (percentage) increase in reported net operating income after loan impairment and other credit risk charges since last year.	**Measure:** (US$) level of basic earnings generated per ordinary share.	**Measure:** (percentage) increase in dividends per share since last year, based on dividends paid in respect of the year to which the dividend relates.
	Target: to deliver consistent growth in risk adjusted revenues.	**Target:** to deliver consistent growth in basic earnings per share.	**Target:** to deliver sustained dividend per share growth.
	Outcome: reported risk-adjusted revenue increased, primarily due to a reversal of adverse movements in previous years on the fair value of own debt designated at fair value and lower loan impairment charges. The latter also drove the increase in underlying risk-adjusted revenue.	**Outcome:** Earnings per share (EPS) increased in 2010, reflecting significantly lower adverse movements on the fair value of own debt due to credit spreads and lower loan impairment charges, which resulted in an increase in reported profit.	**Outcome:** dividends per share increased by 5.9%.

Strategic objectives	Enhance efficiency using economies of scale	Motivate staff to deliver strategy
	Cost efficiency	**Employee engagement**
Key Performance Indicators	**Measure**: (percentage) total operating expenses divided by net operating income	**Measure:** (percentage) measure of employee s emotional and rational

before loan impairment and other credit risk provisions.

Target: to be between 48% and 52%, a range within which business is expected to remain to accommodate both returns to shareholders and the need for continued investment in support of future business growth.

Outcome: the ratio was outside the target range in part due to one-off costs, but also increased investment in operational infrastructure and strategic initiatives.

attachment to HSBC, a combination of advocacy, satisfaction, commitment and pride.

Target: to achieve a 72% global rating in 2010, with progressive improvement to best in class by 2011.

Outcome: 68%, mirroring the fall in global best in class but remaining well above the financial services average.

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Report of the Directors: Overview (continued)

Maintain capital strength and strong liquidity			**Strategic objectives**
Return on average total shareholders equity	**Tier 1 capital**	**Advances to core funding ratio**	
Measure: (percentage) profit attributable to ordinary shareholders divided by average total shareholders equity.	**Measure:** component of regulatory capital comprising core tier 1 and other tier 1 capital.	**Measure:** current loans and advances to customers as a percentage of the total of core customer deposits and term funding with a remaining term to maturity in excess of one year.	**Key Performance Indicators**
Target: to maintain a return in the medium term of between 15% and 19%. In 2011, we intend to replace the target with one in the 12% to 15% range over the normal cycle.	**Target:** to maintain a strong capital base to support the development of the business and meet regulatory capital requirements at all times.	**Target:** to maintain an advances to core funding ratio below limits set for each entity.	
Outcome: return on equity was below the target range, but 4.4 percentage points higher than in 2009.	**Outcome:** the increase in tier 1 capital to 12.1% reflected the contribution of profit to capital, the issue of hybrid capital securities during the year and careful management of RWAs.	**Outcome:** ratio within the limits set by the Risk Management Meeting for each site.	

Reach new customers and expand services to existing customers using the HSBC brand and global network		**Strategic objectives**
Brand perception	**Customer recommendation**	

PFS	Business Banking	PFS	Business Banking	Key Performance Indicators

Measure: an independent survey of brands around the world which judges their relative strength. The results are used to form a brand perception index, where the industry average is zero.

Target: to meet or exceed targets based on performance against key competitors and the industry average.

Outcome: PFS and Business Banking customers judged HSBC s brand to be six points stronger than the competitor average. Our ratings met or exceeded our targets in 2010.

For footnotes, see page 83.

Measure: an independent survey of customers in up to 15 countries which judges how likely they are to recommend a particular brand. The results are used to create a customer recommendation index, where the industry average is zero.

Target: to meet or exceed targets based on performance against key competitors and the industry average.

Outcome: Business Banking exceeded its target. Personal Financial Services fell short of its challenging target, but remained well above the competitor average.

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HSBC HOLDINGS PLC
Report of the Directors: Operating and Financial Review

Financial summary

The management commentary included in the Report of the Directors: Overview and Operating and Financial Review , together with the Employees and Corporate sustainability sections of Governance and the Directors Remuneration Report is presented in compliance with the IFRS Practice Statement Management Commentary *issued by the IASB.*

Reconciliation of reported and underlying profit before tax

We measure our performance internally on a like-for-like basis by eliminating the effects of foreign currency translation differences, acquisitions and disposals of subsidiaries and businesses, and fair value movements on own debt attributable to credit spread where the net result of such movements will be zero upon maturity of the debt; all of which distort year-on-year comparisons. We refer to this as our underlying performance.

Reported results include the effects of the above items. They are excluded when monitoring progress against operating plans and past results because management believes that the underlying basis more accurately reflects operating performance.

Constant currency

Constant currency comparatives for 2009 referred to in the commentaries are computed by retranslating into US dollars for non-US dollar branches, subsidiaries, joint ventures and associates:

- the income statements for 2009 at the average rates of exchange for 2010; and
- the balance sheet at 31 December 2009 at the prevailing rates of exchange on 31 December 2010.

Constant currency comparatives for 2008 referred to in the 2009 commentaries are computed on the same basis, by applying average rates of exchange for 2009 to the 2008 income statement and rates of exchange on 31 December 2009 to the balance sheet at 31 December 2008.

No adjustment has been made to the exchange rates used to translate foreign currency denominated assets and liabilities into the functional currencies of any HSBC branches, subsidiaries, joint ventures or associates. When reference is made to constant currency in tables or commentaries, comparative data reported in the functional currencies of HSBC s operations have been translated at the appropriate exchange rates applied in the current period on the basis described above.

Underlying performance

The tables below compare our underlying performance in 2010 and 2009 with reported profits in those years.

The foreign currency translation differences reflect the relative strengthening of the US dollar against the euro and sterling, which offset its relative weakness against currencies in Asia, Mexico and Brazil during 2010.

The following acquisitions and disposals affected both comparisons:

- the acquisition of PT Bank Ekonomi Raharja Tbk (Bank Ekonomi) in May 2009;
- the gain on sale of our 49% interest in a joint venture for a UK merchant acquiring business in June 2009 of US$280m;
- the gain of US$62m on reclassification of Bao Viet Holdings (Bao Viet) from an available-for-sale asset to an associate in January 2010;
- the gain on sale of our stake in Wells Fargo HSBC Trade Bank in March 2010 of US$66m;
- the gain on disposal of HSBC Insurance Brokers Limited of US$107m in April 2010;
- the dilution gain of US$188m which arose on our holding in Ping An Insurance (Group) Company of China, Limited (Ping An Insurance) following the issue of shares by the company in May 2010;

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Report of the Directors: Operating and Financial Review (continued)

the loss of US$42m on the completion of the sale of our investment in British Arab Commercial Bank plc in October 2010;

the gain on sale of Eversholt Rail Group of US$255m in December 2010; and
the gain of US$74m on the deconsolidation of private equity funds following the management buy-out of Headland Capital Partners Ltd (formally known as HSBC Private Equity (Asia) Ltd) in November 2010.

Reconciliation of reported and underlying profit before tax

	2010 compared with 2009								
HSBC	**2009 as reported US$m**	**2009 adjust-ments[10] US$m**	**Currency translation[11] US$m**	**2009 at 2010 exchange rates[12] US$m**	**2010 as reported US$m**	**2010 adjust-ments[10] US$m**	**2010 under-lying US$m**	**Re-ported change[13] %**	**Under-lying change[13] %**
Net interest income	**40,730**	**(1)**	**642**	**41,371**	**39,441**	**(31)**	**39,410**	**(3)**	**(5)**
Net fee income	**17,664**	**(210)**	**182**	**17,636**	**17,355**	**(3)**	**17,352**	**(2)**	**(2)**
Changes in fair value[14]	**(6,533)**	**6,533**			**(63)**	**63**		**99**	
Other income	**14,320**	**(283)**	**228**	**14,265**	**11,514**	**(719)**	**10,795**	**(20)**	**(24)**
Net operating income[15]	**66,181**	**6,039**	**1,052**	**73,272**	**68,247**	**(690)**	**67,557**	**3**	**(8)**
Loan impairment charges and other credit risk provisions	**(26,488)**		**(330)**	**(26,818)**	**(14,039)**		**(14,039)**	**47**	**48**
Net operating income	**39,693**	**6,039**	**722**	**46,454**	**54,208**	**(690)**	**53,518**	**37**	**15**
Operating expenses	**(34,395)**	**200**	**(568)**	**(34,763)**	**(37,688)**	**19**	**(37,669)**	**(10)**	**(8)**
Operating profit	**5,298**	**6,239**	**154**	**11,691**	**16,520**	**(671)**	**15,849**	**212**	**36**

Income from associates	**1,781**	**(1)**	**11**	**1,791**	**2,517**		**2,517**	**41**	**41**
Profit before tax	**7,079**	**6,238**	**165**	**13,482**	**19,037**	**(671)**	**18,366**	**169**	**36**
By geographical region									
Europe	**4,009**	**2,546**	**(152)**	**6,403**	**4,302**	**(164)**	**4,138**	**7**	**(35)**
Hong Kong	**5,029**	**1**	**(10)**	**5,020**	**5,692**	**(130)**	**5,562**	**13**	**11**
Rest of Asia-Pacific	**4,200**	**3**	**205**	**4,408**	**5,902**	**(211)**	**5,691**	**41**	**29**
Middle East	**455**		**(2)**	**453**	**892**	**42**	**934**	**96**	**106**
North America	**(7,738)**	**3,688**	**46**	**(4,004)**	**454**	**(208)**	**246**		
Latin America	**1,124**		**78**	**1,202**	**1,795**		**1,795**	**60**	**49**
Profit before tax	**7,079**	**6,238**	**165**	**13,482**	**19,037**	**(671)**	**18,366**	**169**	**36**
By customer group and global business									
Personal Financial Services	**(2,065)**	**(2)**	**(70)**	**(2,137)**	**3,518**	**(10)**	**3,508**		
Commercial Banking	**4,275**	**(306)**	**64**	**4,033**	**6,090**	**(133)**	**5,957**	**42**	**48**
Global Banking and Markets	**10,481**	**13**	**173**	**10,667**	**9,536**	**(342)**	**9,194**	**(9)**	**(14)**
Global Private Banking	**1,108**		**1**	**1,109**	**1,054**	**1**	**1,055**	**(5)**	**(5)**
Other	**(6,720)**	**6,533**	**(3)**	**(190)**	**(1,161)**	**(187)**	**(1,348)**	**83**	**(609)**
Profit before tax	**7,079**	**6,238**	**165**	**13,482**	**19,037**	**(671)**	**18,366**	**169**	**36**

For footnotes, see page 83.
Additional information is available on pages 47(a) to 47(f) and 80(b) to 80(g).

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HSBC HOLDINGS PLC
Report of the Directors: Operating and Financial Review (continued)

Consolidated income statement

Five-year summary consolidated income statement

	2010 US$m	2009 US$m	2008 US$m	2007 US$m	2006 US$m
Net interest income	**39,441**	40,730	42,563	37,795	34,486
Net fee income	**17,355**	17,664	20,024	22,002	17,182
Net trading income	**7,210**	9,863	6,560	9,834	8,222
Net income/(expense) from financial instruments designated at fair value	**1,220**	(3,531)	3,852	4,083	657
Gains less losses from financial investments	**968**	520	197	1,956	969
Gains arising from dilution of interests in associates	**188**			1,092	
Dividend income	**112**	126	272	324	340
Net earned insurance premiums	**11,146**	10,471	10,850	9,076	5,668
Gains on disposal of French regional banks			2,445		
Other operating income	**2,374**	2,788	1,808	1,439	2,546
Total operating income	**80,014**	78,631	88,571	87,601	70,070
Net insurance claims incurred and movement in liabilities to policyholders	**(11,767)**	(12,450)	(6,889)	(8,608)	(4,704)
Net operating income before loan impairment charges and other credit risk provisions	**68,247**	66,181	81,682	78,993	65,366
Loan impairment charges and other credit risk provisions	**(14,039)**	(26,488)	(24,937)	(17,242)	(10,573)
Net operating income	**54,208**	39,693	56,745	61,751	54,793
Total operating expenses[17]	**(37,688)**	(34,395)	(49,099)	(39,042)	(33,553)
Operating profit	**16,520**	5,298	7,646	22,709	21,240

Share of profit in associates and joint ventures	**2,517**	1,781	1,661	1,503	846
Profit before tax	**19,037**	7,079	9,307	24,212	22,086
Tax expense	**(4,846)**	(385)	(2,809)	(3,757)	(5,215)
Profit for the year	**14,191**	6,694	6,498	20,455	16,871
Profit attributable to shareholders of the parent company	**13,159**	5,834	5,728	19,133	15,789
Profit attributable to non-controlling interests	**1,032**	860	770	1,322	1,082

Five-year financial information

	US$	US$	US$	US$	US$
Basic earnings per share[18]	**0.73**	0.34	0.41	1.44	1.22
Diluted earnings per share[18]	**0.72**	0.34	0.41	1.42	1.21
Dividends per share[1]	**0.34**	0.34	0.93	0.87	0.76
	%	%	%	%	%
Dividend payout ratio[19]	**46.6**	100.0	226.8	60.4	62.3
Post-tax return on average total assets	**0.57**	0.27	0.26	0.97	1.00
Return on average total shareholders equity	**9.5**	5.1	4.7	15.9	15.7
Average foreign exchange translation rates to US$:					
US$1: £	**0.648**	0.641	0.545	0.500	0.543
US$1:	**0.755**	0.719	0.684	0.731	0.797

For footnotes, see page 83.

Reported profit before tax of US$19.0bn in 2010 was 169% higher than in 2009, and 36% higher on an underlying basis. The difference between reported and underlying results is explained on page 14. Except where stated otherwise, the commentaries in the Financial Summary are on an underlying basis and references to HSBC Finance and HSBC Bank USA are on a management basis, rather than a legal entity basis (for details see page 37).

Net operating income before loan impairment charges and other credit risk provisions (revenue) was lower than in 2009, notably due to a decline in balances in North America, lower trading income from adverse movements on non-qualifying hedges and a fall in revenue from GB&M. In the former, we continued to reposition our core businesses and we remained focused on managing down our run-off portfolios. As a consequence, revenue fell, reflecting declining balances in the run-off portfolios and in the Card and Retail Services business, where revenue was also adversely affected by new regulations. In GB&M, lower revenue was generated in Balance Sheet Management as higher yielding positions matured and funds were invested in lower yielding assets. Trading income declined driven by increased competition and reduced margins across core products, and less favourable market conditions caused by the European sovereign debt crisis. These factors were partly offset by increased CMB revenue from balance sheet growth, particularly in Asia, and higher trade-related fees.

Loan impairment charges were significantly lower than in 2009, with decreases across all regions and customer groups as economic conditions improved. The most significant decline in loan impairment charges was in North America, reflecting lower balances due to increased repayments, an improvement in delinquency rates in Card and Retail Services, and the continued run-off of balances in the Consumer Finance business. There were also marked declines in the Middle East and in
Latin America, primarily in Mexico and Brazil, reflecting a reduction in personal lending balances as selected portfolios were managed down, and an improvement in credit quality as origination criteria were tightened and collection practices improved. In GB&M, loan impairment charges were significantly lower, reflecting the improvement in the credit environment which resulted in fewer significant charges than those taken in 2009 in relation to a small number of clients, notably in Europe and other credit risk provisions fell in the available-for-sale asset-backed securities (ABS) portfolio due to a slowing in the rate of anticipated losses in the underlying collateral pools.

Underlying profit before tax rose by 36% as a significant fall in impairment charges offset a decline in revenue.

Operating expenses were higher than in 2009, in part due to specific one-off items such as a US$0.3bn charge for UK bank payroll tax in 2010 and the non-recurrence of a pension accounting gain of US$0.5bn in 2009 relating to the treatment of staff benefits. Excluding these items, operating expenses rose in support of strategic growth initiatives in our target markets to invest in operational infrastructure and the selective recruitment of customer-facing staff.

Income from associates increased, driven by strong results in Asia which reflected robust economic growth in mainland China.

In 2010, taxable profits were achieved in the US, principally as the result of a gain from an internal reorganisation that was not recognised for accounting purposes which increased the effective tax rate by 6.4 percentage points. If this were excluded, the effective tax rate would be 19.1% which is in line with our geographical range of business activities. Reported profit after tax was US$7.5bn higher than in 2009.

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HSBC HOLDINGS PLC
Report of the Directors: Operating and Financial Review (continued)

Group performance by income and expense item

Net interest income

	2010 US$m	2009 US$m	2008 US$m
Interest income	**58,345**	62,096	91,301
Interest expense	**(18,904)**	(21,366)	(48,738)
Net interest income[20]	**39,441**	40,730	42,563
Average interest-earning assets	**1,472,294**	1,384,705	1,466,622
Gross interest yield[21]	**3.96%**	4.48%	6.23%
Net interest spread[22]	**2.55%**	2.90%	2.87%
Net interest margin[23]	**2.68%**	2.94%	2.90%

Summary of interest income by type of asset

	2010			2009			2008		
	Average balance US$m	**Interest income US$m**	**Yield %**	Average balance US$m	Interest income US$m	Yield %	Average balance US$m	Interest income US$m	Yield %
Short-term funds and loans and advances to banks	**236,742**	**4,555**	**1.92**	192,578	4,199	2.18	240,111	9,646	4.02
Loans and advances to customers	**858,499**	**44,186**	**5.15**	870,057	48,301	5.55	943,662	68,722	7.28
Financial investments	**378,971**	**9,375**	**2.47**	322,880	9,425	2.92	264,396	12,618	4.77
Other interest-earning assets[24]	**(1,918)**	**229**	**(11.94)**	(810)	171	(21.11)	18,453	315	1.71
Total interest-earning assets	**1,472,294**	**58,345**	**3.96**	1,384,705	62,096	4.48	1,466,622	91,301	6.23
Trading assets[25]	**332,511**	**6,027**	**1.81**	357,504	7,614	2.13	428,539	16,742	3.91
Financial assets designated at fair value[26]	**52,692**	**1,033**	**1.96**	62,143	1,032	1.66	37,303	1,108	2.97
	(22,905)			(26,308)			(20,360)		

Impairment provisions									
Non-interest-earning assets	**664,308**			667,942			596,885		
Total assets and interest income	**2,498,900**	**65,405**	**2.62**	2,445,986	70,742	2.89	2,508,989	109,151	4.35

Summary of interest expense by type of liability and equity

	2010			2009			2008		
	Average balance US$m	**Interest expense US$m**	**Cost %**	Average balance US$m	Interest expense US$m	Cost %	Average balance US$m	Interest expense US$m	Cost %
Deposits by banks[27]	**111,443**	**1,136**	**1.02**	117,847	1,659	1.41	135,747	4,959	3.65
Financial liabilities designated at fair value own debt issued[28]	**66,706**	**1,271**	**1.91**	60,221	1,558	2.59	63,835	3,133	4.91
Customer accounts[29]	**962,613**	**10,778**	**1.12**	940,918	11,346	1.21	950,854	27,989	2.94
Debt securities in issue	**189,898**	**4,931**	**2.60**	225,657	5,901	2.62	286,827	11,982	4.18
Other interest-bearing liabilities	**8,730**	**788**	**9.03**	8,640	902	10.44	14,579	675	4.63
Total interest-bearing liabilities	**1,339,390**	**18,904**	**1.41**	1,353,283	21,366	1.58	1,451,842	48,738	3.36
Trading liabilities	**258,348**	**3,497**	**1.35**	205,670	3,987	1.94	277,940	11,029	3.97
Financial liabilities designated at fair value (excluding own debt issued)	**17,456**	**283**	**1.62**	15,688	293	1.87	21,266	345	1.62
Non-interest bearing current accounts	**142,579**			123,271			98,193		
Total equity and other non-interest bearing liabilities	**741,127**			748,074			659,747		
Total equity and liabilities	**2,498,900**	**22,684**	**0.91**	2,445,986	25,646	1.05	2,508,988	60,112	2.40

For footnotes, see page 83.

Reported net interest income fell by 3% to US$39bn; the decline was 5% on an underlying basis. This was driven by the exceptionally low interest rate environment and by the effect of repositioning our customer assets towards secured lending as we reduced our higher risk and higher yielding portfolios.

Revenues in Balance Sheet Management decreased, as expected, from the strong levels of 2009 as higher yielding positions taken in prior years matured and opportunities for reinvestment at equivalent yields were limited by the prevailing low interest rates and flatter yield curves.

The fall in income from interest-earning assets was driven by declining yields on loans and advances to customers following the Group s decision to reposition the lending portfolio towards higher quality assets. Higher yielding unsecured lending balances decreased, particularly in North America, where the run-off portfolios continued to diminish and credit card balances fell as the number of active accounts declined and repayments by customers increased. Certain higher risk portfolios were also managed down in Latin America, Asia and the Middle East. This reduction was partly offset by commercial lending growth in CMB and GB&M, and growth in secured lending in the UK in residential mortgages.

The interest expense on debt issued by the Group fell, largely due to a decline in average balances in debt securities in issue as HSBC Finance s funding requirements continued to decrease in line with the run-off of the residual balances in Mortgage Services and Consumer
Lending and the sale of the vehicle finance portfolios.

Net interest income includes the expense of the internal funding of trading assets, while related revenue is reported in trading income. The cost of funding these assets declined as a result of the low interest rates. In reporting our customer group results, this cost is included within net trading income.

Net interest spread decreased due to lower yields on loans and advances to customers, partly as a result of the greater focus on secured lending. In addition, returns on financial investments and deposit spreads remained constrained due to low interest rates. Our net interest margin fell by a lesser amount due to the benefit from an increase in net free funds as customers held more funds in liquid non-interest bearing current accounts in the current low interest rate environment.

Net fee income

	2010 US$m	2009 US$m	2008 US$m
Cards	**3,801**	4,625	5,844
Account services	**3,632**	3,592	4,353
Funds under management	**2,511**	2,172	2,757
Broking income	**1,789**	1,617	1,738
Credit facilities	**1,635**	1,479	1,313
Insurance	**1,147**	1,421	1,771
Imports/exports	**991**	897	1,014
Global custody	**700**	988	1,311
Remittances	**680**	613	610
Underwriting	**623**	746	325
Unit trusts	**560**	363	502
Corporate finance	**440**	396	381
Trust income	**291**	278	325
Mortgage servicing	**118**	124	120
Maintenance income on operating leases	**99**	111	130
Taxpayer financial services	**73**	87	168
Other	**2,027**	1,894	2,102

Fee income	**21,117**	21,403	24,764
Less: fee expense	**(3,762)**	(3,739)	(4,740)
Net fee income	**17,355**	17,664	20,024

Net fee income marginally decreased compared with 2009 on both a reported and an underlying basis. The significant decrease in fee income in North America, primarily in Card and Retail Services, was mostly offset by higher investment-related fees in Asia and Europe and an increase in trade-related fee income in Asia.

The significant fall in fee income from cards occurred primarily in North America, driven by lower volumes, improved delinquency rates and the revision to charging practices following the implementation of the Credit Card Accountability, Responsibility and Disclosure Act (CARD Act).

Insurance fee income was markedly down. In the US, the decline resulted from lower sales of credit protection products associated with the cards business. In the UK, income was lower on a reported basis due to the sale of the insurance brokerage business in the first half of 2010.

Overall, underwriting fee income declined, particularly in Europe as a result of reduced capital market activity in the uncertain economic environment, although in Asia underwriting fees increased following several notable transactions.

Net fee income from sales of investment products in Asia and Europe increased, driven by a stronger investment performance in funds and improved customer sentiment which led to higher volumes.

Credit facilities fees also rose, notably in Asia, as a result of an increase in loan syndication transactions completed during the year.

Net fee income from trade finance also increased, particularly in Asia, reflecting a rise in trade activity.

Net trading income

	2010 US$m	2009 US$m	2008 US$m
Trading activities	**5,708**	5,312	2,988
Net interest income on trading activities	**2,530**	3,627	5,713
Other trading income hedge ineffectiveness:			
on cash flow hedges	**(9)**	90	(40)
on fair value hedges	**38**	(45)	5
Non-qualifying hedges	**(1,057)**	951	(1,122)
Losses on Bernard L. Madoff Investment Securities LLC fraud		(72)	(984)
Net trading income[30,31]	**7,210**	9,863	6,560

For footnotes, see page 83.

Reported net trading income was US$7.2bn, 27% lower than in 2009. On an underlying basis, net trading income declined by 28% due to adverse movements on non-qualifying hedges and lower income from trading activities.

A US$1.1bn adverse fair value movement was reported on non-qualifying hedges compared with a favourable fair value movement of US$954m in 2009. These instruments are derivatives entered into as part of a documented interest rate management strategy for which hedge accounting was not, or could not be, applied. They are principally cross-currency and interest rate swaps used to economically hedge fixed rate debt issued by HSBC Holdings, floating rate debt issued by HSBC Finance and certain operating leased assets. The loss recognised on non-qualifying hedges was a result of fair value losses on these instruments, driven by the decrease in long-term US interest rates relative to sterling and euro rates. In HSBC Finance, the volume of non-qualifying hedge positions also increased as the duration of the mortgage book lengthened and swaps were used to align more closely the duration of the funding liabilities. The size and direction of the changes in fair value of non-qualifying hedges which are recognised in the income statement can be volatile from year to year, but do not alter the cash flows expected as part of the documented interest rate management strategy for both the instruments and the underlying economically hedged assets and liabilities.

The remaining decline in net trading income was driven by increased competition and reduced margins across core products. European sovereign debt concerns and increased economic uncertainty resulted in less favourable market conditions compared with 2009.

In the Credit business, corporate bond trading volumes remained robust following investment in electronic trading capabilities, though revenues were affected as margins declined and credit spread movements were more favourable in

2009. This was partly offset by gains on the legacy portfolio which included a net release of write-downs on legacy positions and monoline credit exposures of US$429m. This compared with a reported write-down of US$331m in 2009.

Rates income decreased, reflecting reduced margins and increased risk aversion from customers due to economic uncertainty. Turmoil in the eurozone led to sovereign debt downgrades and falling asset prices in certain European countries, leading to lower revenues in the trading portfolio. These factors were partly offset by a small favourable fair value movement on structured liabilities, compared with an adverse movement in 2009.

Lower net trading income was driven by a US$2.0bn adverse movement on non-qualifying hedges from 2009.

Performance in the Foreign Exchange business remained strong, although was affected by a competitive trading environment and tighter bid-offer spreads as competitors sought to rebuild their businesses. In addition, revenues fell as market volatility declined from the exceptional levels seen in early 2009.

The Equities business continued to increase market share in its target markets, following

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investment in the equities platform. However, core revenues fell, as overall market volumes and margins declined.

Trading income benefited from foreign exchange gains on trading assets held as economic hedges of foreign currency debt designated at fair value compared with losses on these instruments in 2009. These gains were largely offset by
corresponding losses reported in Net income from financial instruments designated at fair value .

Net interest income earned on trading activities decreased by 30%, driven by reduced holdings of debt securities. The cost of internally funding these assets also declined, but this interest expense is reported under Net interest income and excluded from net trading income.

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

	2010 US$m	2009 US$m	2008 US$m
Net income/(expense) arising from:			
financial assets held to meet liabilities under insurance and investment contracts	**2,349**	3,793	(5,064)
liabilities to customers under investment contracts	**(946)**	(1,329)	1,751
HSBC s long-term debt issued and related derivatives	**(258)**	(6,247)	6,679
Change in own credit spread on long-term debt	**(63)**	(6,533)	6,570
Other changes in fair value[32]	**(195)**	286	109
other instruments designated at fair value and related derivatives	**75**	252	486
Net income/(expense) from financial instruments designated at fair value	**1,220**	(3,531)	3,852

Assets and liabilities from which net income/(expense) from financial instruments designated at fair value arose

	2010 US$m	2009 US$m	2008 US$m
Financial assets designated at fair value at 31 December	**37,011**	37,181	28,533
Financial liabilities designated at fair value at 31 December	**88,133**	80,092	74,587
Including:			
Financial assets held to meet liabilities under:			
insurance contracts and investment contracts with DPF[33]	**7,167**	6,097	5,556
unit-linked insurance and other insurance and investment contracts	**19,725**	16,982	12,758

Long-term debt issues designated at fair value	**69,906**	62,641	58,686

For footnotes, see page 83.

The accounting policies for the designation of financial instruments at fair value and the treatment of the associated income and expenses are described in Notes 2i and 2b on the Financial Statements, respectively.

The majority of the financial liabilities designated at fair value relate to certain fixed-rate long-term debt issues whose rate profile has been changed to floating through interest rate swaps as part of a documented interest rate management strategy. The movement in fair value of these long-term debt issues includes the effect of our credit spread changes and any ineffectiveness in the economic relationship between the related swaps and own debt. As credit spreads widen or narrow, accounting profits or losses, respectively, are booked. The size and direction of the changes in the credit spread on our debt and ineffectiveness, which are recognised in the income statement, can be volatile from year to year, but do not alter the cash flows envisaged as part of the documented interest rate management strategy. As a consequence, fair value movements arising from changes in our own credit spread on long-term debt and other fair value movements on the debt and related derivatives are not regarded internally as part of managed performance and are therefore not allocated to customer groups, but are reported in Other . Credit spread movements on own debt are excluded from underlying results, and related fair value movements are not included in the calculation of regulatory capital.

We reported net income from financial instruments designated at fair value of US$1.2bn in 2010 compared with a net expense of US$3.5bn in 2009. On an underlying basis, the equivalent figures were income of US$1.3bn in 2010 and US$2.9bn in 2009. The difference between the reported and underlying results arises from the exclusion from the latter of the credit spread-related movements in the fair value of our own long-term debt, on which we reported adverse fair value movements of US$63m in 2010 and US$6.5bn in 2009. In North America, a small favourable fair value movement was reported in 2010 as credit spreads widened marginally, in contrast with a significant adverse fair value movement in 2009. In Europe, significantly lower adverse fair value movements were reported in 2010 as credit spreads tightened, but to a lesser extent than in the previous year.

Income arising from financial assets held to meet liabilities under insurance and investment contracts reflected lower investment gains as the growth in equity markets was less than that of 2009. This predominantly affected the value of assets held to support unit-linked contracts in the UK, Hong Kong, Singapore and Brazil and participating contracts in France.

For investment gains or losses related to assets held to back investment contracts, the corresponding movement in liabilities to customers is also recorded under Net income from financial instruments designated at fair value .

Investment gains or losses related to assets held to back insurance contracts or investment contracts with discretionary participation features (DPF) are offset by a corresponding change in Net insurance claims incurred and movement in liabilities to policyholders to reflect the extent to which unit-linked policyholders, in particular, participate in the investment performance of the associated asset portfolios.

Gains less losses from financial investments

	2010 US$m	2009 US$m	2008 US$m
Net gains/(losses) from disposal of:			
debt securities	**564**	463	19
equity securities	**516**	407	1,216
other financial investments	**(7)**	8	4
	1,073	878	1,239
Impairment of available-for-sale equity securities	**(105)**	(358)	(1,042)
Gains less losses from financial investments	**968**	520	197

Reported gains less losses from financial investments increased by US$448m to US$968m. On an underlying basis, excluding an accounting gain arising from the reclassification of Bao Viet as an associate following our purchase of additional shares, they increased by 69%. This was driven by a decrease in the level of impairments on available-for-sale equity investments as market values improved, along with an increase in gains on the disposal of equity and debt securities.

Impairments on equity investments declined markedly compared with 2009 as the improving economic situation resulted in a reduction in the level of write-downs required on private equity and other strategic equity investments.

Higher net gains were reported in Balance Sheet Management on disposals of available-for-sale debt securities, mainly in Europe and Asia. These were partly offset by a decrease in North America, where net gains realised from the sale of mortgage-backed securities and other ABSs in 2009 did not recur.

Net gains on the disposal of equity securities increased, primarily in our private equity portfolio in Europe, as the market offered greater opportunities for divestment. This was partly offset by the non-recurrence of the gain on disposal of our holdings of Visa Inc. shares in 2009.

Net earned insurance premiums

	2010 US$m	2009 US$m	2008 US$m
Gross insurance premium income	**11,609**	10,991	12,547
Reinsurance premiums	**(463)**	(520)	(1,697)
Net earned insurance premiums	**11,146**	10,471	10,850

Net earned insurance premiums increased by 6% to US$11.1bn on both a reported and an underlying basis.

Growth was largely attributable to the continued strong performance of life insurance products in Asia. Successful sales campaigns and the recruitment of additional insurance sales managers increased net earned premiums in Hong Kong, particularly from deferred annuity and unit-linked products, and a life insurance product designed for high net worth individuals. Higher sales were also reported in Malaysia, Taiwan and mainland China, primarily from successful product launches and marketing campaigns.

Net earned premiums in Latin America increased marginally in the improved economic conditions, driven by higher sales in Brazil, Argentina and Mexico and repricing initiatives in Argentina.

In France, an increase in sales of investment contracts with DPF drove higher net earned premiums. Strong sales activity also led to higher net earned premiums in our UK life insurance business.

This growth was partly offset by a reduction in non-life insurance premiums, primarily due to the run-off of the legacy motor book in the UK, which was closed during the second half of 2009, and the decision taken during 2010 not to renew certain contracts in the Irish business.

Net earned premiums in North America also decreased, reflecting a decline in sales of payment protection products following the discontinuation of mortgage originations in HSBC Finance.

Other operating income

	2010 US$m	2009 US$m	2008 US$m
Rent received	**535**	547	606
Losses recognised on assets held for sale	**(263)**	(115)	(130)
Valuation gains/(losses) on investment properties	**93**	(24)	(92)
Gain on disposal of property, plant and equipment, intangible assets and non-financial investments	**889**	1,033	881
Change in present value of in-force long-term insurance business	**705**	605	286
Other	**603**	742	257
Other operating income	**2,562**	2,788	1,808

Reported other operating income of US$2.6bn was 8% lower than in 2009. Income in 2010 included gains of US$188m following the dilution of our holding in Ping An Insurance, US$107m from the sale of HSBC Insurance Brokers, US$66m from the disposal of our interest in the Wells Fargo HSBC Trade Bank and US$255m from the sale of Eversholt Rail Group. In addition, we reported a gain of US$74m resulting from the sale of HSBC Private Equity (Asia) Ltd, partly offset by a loss of US$42m on the disposal of our shareholding in British Arab Commercial Bank plc. Reported results in 2009 included a gain of US$280m from the sale of the remaining stake in the card merchant-acquiring business in the UK.

On an underlying basis, excluding the items referred to above, other operating income decreased by 23%, primarily because gains on the sale of properties in London and Hong Kong in 2009 did not recur.

Net losses recognised on assets held for sale increased, reflecting a US$207m loss on the sale of the US vehicle finance servicing operation and associated US$5.3bn loan portfolio.

Net investment valuation gains on investment properties contrasted with losses in 2009. This reflected improvements in the property markets in Hong Kong and the UK which led to net valuation gains on investment properties, compared with net valuation losses in 2009.

A loss on sale of the US vehicle finance business contributed to a fall in Other operating income.

We recognised gains of US$194m and US$56m in 2010 on the sale and leaseback of our Paris and New York headquarters buildings, respectively. These compared with more substantial underlying gains of US$667m (US$686m as reported) on the sale and leaseback of 8 Canada Square and the sale of a property in Hong Kong in 2009.

Strong sales of life insurance products, notably in Hong Kong, resulted in favourable movements in the present value of in-force (PVIF) long-term insurance business. These were offset in part by the non-recurrence of gains recognised in 2009 following the refinement of the income recognition methodology in HSBC Finance.

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Net insurance claims incurred and movement in liabilities to policyholders

	2010 US$m	2009 US$m	2008 US$m
Insurance claims incurred and movement in liabilities to policyholders:			
gross	**11,969**	12,560	9,206
reinsurers share	**(202)**	(110)	(2,317)
net[34]	**11,767**	12,450	6,889

For footnote, see page 83.

Net insurance claims incurred and movement in liabilities to policyholders decreased by 5% and 4% on a reported and an underlying basis, respectively.

Lower investment returns than in 2009, particularly in Asia, Europe and Brazil, led to a decrease in the movement in liabilities to policyholders on unit-linked insurance contracts and, to a certain extent, participating contracts, whose policyholders share in the investment performance of the assets supporting their policies. The gains or losses experienced on the financial assets designated at fair value held to support insurance contract liabilities and investment contracts with DPF are reported in Net income from financial instruments designated at fair value .

In Asia, the effect of the lower investment returns was more than offset by additional reserves established for new business written, consistent with the increase in net insurance premiums earned, particularly in Hong Kong, as a result of successful sales campaigns and the recruitment of additional insurance sales managers.

In addition, the increase in reserves in 2009 on the now closed UK motor insurance book, which reflected the rising incidence and severity of claims at that time, did not recur. The decision taken in 2010 not to renew certain contracts in our Irish business resulted in a further decrease in net insurance claims incurred and movement in liabilities to policyholders.

Loan impairment charges and other credit risk provisions

	2010 US$m	2009 US$m	2008 US$m
Loan impairment charges			
New allowances net of allowance releases	**14,568**	25,832	24,965
Recoveries of amounts previously written off	**(1,020)**	(890)	(834)
	13,548	24,942	24,131
Individually assessed allowances	**2,625**	4,458	2,064
Collectively assessed allowances	**10,923**	20,484	22,067

Impairment of available-for-sale debt securities	**472**	1,474	737
Other credit risk provisions	**19**	72	69
Loan impairment charges and other credit risk provisions	**14,039**	26,488	24,937
	%	%	%
as a percentage of net operating income excluding the effect of fair value movements in respect of credit spread on own debt and before loan impairment charges and other credit risk provisions	**20.6**	36.4	33.2
Impairment charges on loans and advances to customers as a percentage of gross average loans and advances to customers	**1.5**	2.8	2.5
	US$m	US$m	US$m
Customer impaired loans	**28,091**	30,606	25,352
Customer loan impairment allowances	**20,083**	25,542	23,909

On a reported basis, loan impairment charges and other credit risk provisions were US$14bn, a decline of 47% compared with 2009 and 48% on an underlying basis. There was improvement across all regions and in all customer groups.

At 31 December 2010, the aggregate balance of customer loan impairment allowances was US$20.1bn. This represented 2.2% of gross loans and advances to customers (net of reverse repos and settlement accounts) compared with 3.0% at 31 December 2009.

We actively managed down some of our higher risk portfolios in all regions and enhanced credit quality through tighter underwriting and increased focus on the sale of secured products to customers where we already held a banking relationship. Loan impairment charges in our CMB and GB&M businesses fell as economic conditions improved and we recognised fewer large loan impairment charges against specific clients than in 2009.

Loan impairment charges and other credit risk provisions of US$14bn were 48% or US$12.8bn lower than in 2009.

Impairments on available-for-sale debt securities declined markedly to US$472m from the US$1.5bn reported in 2009, mainly reflecting a slowing in the rate of anticipated losses in the underlying collateral pools.

The most significant decline in loan impairment charges was in our HSBC Finance portfolios in **the US**, where lending balances reduced and delinquency levels improved.

Loan impairment charges and other credit risk provisions in the US declined by 48% to US$7.9bn, the lowest level since 2006, representing 57% of the Group s total reduction compared with 2009. This mainly occurred in the US PFS business, where loan impairment charges declined by US$6.1bn to US$8.0bn, primarily in the Card and Retail Services business of HSBC Finance and, to a lesser extent, in the run-off consumer finance portfolios.

In Cards and Retail Services, loan impairment charges declined by 57% to US$2.2bn. This improvement reflected the continuing effects of additional steps taken from the fourth quarter of 2007 to manage risk, including tightening underwriting criteria, lowering credit limits and reducing the number of active cards. An increased focus by our customers on reducing outstanding credit card debt helped improve delinquency levels.

Loan impairment charges in our Consumer Lending and Mortgage Services businesses declined by 29% to US$5.7bn, due to the continued run-off of lending balances in these portfolios and lower delinquency balances. Total loss severities on foreclosed loans improved compared with 2009, reflecting an increase in the number of properties for which we accepted a deed in lieu of foreclosure or a short sale, both of which result in lower losses compared with loans which are subject to a formal foreclosure process.

During 2010, state and federal prosecutors announced investigations into foreclosure practices of certain mortgage service providers. As a result, we expect that the scrutiny of documents will increase, and in some states additional verification of information will be required. If these trends continue there may be delays in their processing. See page 83 for more information on the investigation into US foreclosure practices.

In HSBC Bank USA, loan impairment charges in PFS fell by 92% to US$50m, reflecting lower lending balances and improved credit quality in the residential mortgage portfolio.

In GB&M in the US, a net release of loan impairment charges and other credit risk provisions reflected the improved credit environment and a release of impairments of available-for-sale ABSs as mentioned previously. In CMB, loan impairment charges declined by US$194m as the improved economic conditions resulted in credit upgrades on certain accounts, and fewer downgrades across all business lines.

In **the UK**, loan impairment charges in PFS and CMB declined as economic conditions improved and interest rates remained at low levels, resulting in an improvement in delinquency levels. In PFS, loan impairment charges fell by 35% to US$1.1bn as we actively reduced our exposure to unsecured lending, while collections increased mainly due to programmes implemented to improve performance. In the UK secured lending book, credit quality continued to be high and loan impairment charges remained at low levels. In CMB, loan impairment charges declined by US$159m due to strengthened credit risk management and improved collections, notably in the UK property, retail and service sectors.

Loan impairment charges and other credit provisions fell markedly in GB&M reflecting the improved credit outlook, loan restructuring activity and the non-recurrence of significant charges against a small number of clients in the financial and property sectors. Credit risk provisions on certain available-for-sale ABSs also reduced.

Loan impairment charges and other credit risk provisions in **Latin America** declined by 44% to US$1.5bn. In PFS, loan impairment charges of US$1.2bn were 45% lower, mainly in Mexico due to a reduction in balances and improved delinquency rates in our credit card portfolio. In Brazil, they also declined as we managed down the size of certain consumer finance portfolios and economic conditions improved. In 2010, initiatives taken in the region to improve the quality of the loan portfolios continued. These steps included the tightening of underwriting criteria, reducing and, in some instances, eliminating the use of higher risk, non-branch sales channels, and continued investment in our collections infrastructure. In our CMB portfolios, loan impairment charges and other credit risk provisions declined by 50% to US$293m, as improved economic conditions and credit quality resulted in lower specific impairment charges in all sectors.

In the **Middle East**, loan impairment charges and other credit risk provisions fell by 53% to US$627m as lower loan impairment charges in both PFS and CMB were partly offset by an increase in GB&M following restructuring activities. In our PFS business, loan impairment charges declined by 61% to US$227m, reflecting a marked decline in delinquency levels and lower lending balances, particularly in our credit card and unsecured personal lending book, as a result of managing down higher risk portfolios. Credit limits were tightened and our customer acquisition strategy was revised in the region to concentrate on Premier and Advance customers. This resulted in an improvement in credit quality. In CMB, lower loan impairment charges reflected a reduction in collective impairment charges and fewer specific loan impairment charges as economic conditions improved.

In **Rest of Asia-Pacific**, loan impairment charges declined as the credit environment improved. In India, loan impairment charges fell by 83% to US$82m, mainly in PFS as certain unsecured lending portfolios and the higher risk elements of the credit card portfolio were managed down, and economic conditions improved. Impairment charges also declined in CMB, due to the non-recurrence of charges against specific technology-related exposures in 2009. Partly offsetting these increases were higher specific loan impairment charges in GB&M.

In **Hong Kong**, loan impairment charges fell by 77% to US$114m, as economic conditions improved and fewer large specific loan impairment charges were reported against the CMB and GB&M portfolios. Loan impairment charges fell in PFS too, mainly on unsecured lending as unemployment and bankruptcy levels reduced.

Operating expenses

	2010 US$m	2009 US$m	2008 US$m
By expense category			
Employee compensation and benefits	**19,836**	18,468	20,792
Premises and equipment (excluding depreciation and impairment)	**4,348**	4,099	4,305
General and administrative expenses	**10,808**	9,293	10,955
Administrative expenses	**34,992**	31,860	36,052
Depreciation and impairment of property, plant and equipment	**1,713**	1,725	1,750
Amortisation and impairment of intangible assets	**983**	810	733
Goodwill impairment			10,564
Operating expenses	**37,688**	34,395	49,099

Staff numbers (full time equivalents)

	At 31 December		
	2010	2009	2008
Europe	**75,698**	76,703	82,093
Hong Kong	**29,171**	27,614	29,330
Rest of Asia-Pacific	**91,607**	87,141	89,706
Middle East	**8,676**	8,281	8,453
North America	**33,865**	35,458	44,725
Latin America	**56,044**	54,288	58,559
Staff numbers	**295,061**	289,485	312,866

Operating expenses increased by 10% to US$37.7bn on a reported basis and by 8% on an underlying basis. Significant one-off items included aggregate payroll taxes of US$324m levied on 2009 bonuses in the UK and France, and the curtailment of certain benefits delivered through pension schemes, which generated accounting credits of US$148m in the US and US$480m (US$499m as reported) in the UK in 2010 and 2009, respectively. Excluding these items, expenses grew by 6% as we continued to invest in our operational infrastructure, customer-facing and support staff, and GB&M s capabilities and platforms.

Employee compensation and benefits increased by 7%, partly due to the net effect of the curtailment gains and the payroll tax referred to above.

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Excluding these items, staff costs rose by 3%. Performance-related costs increased, primarily in Asia, reflecting improved business performance and increased staff numbers. While year-end staff numbers increased as the pace of recruitment accelerated in the second half of the year, average staff numbers remained below 2009 levels. The growth in staff numbers in Asia encompassed both customer-facing and back-office staff supporting business growth and increased operational capacity. In Latin America, staff costs grew following union-agreed salary increases and the recruitment of customer-facing and regional support staff, primarily in the latter part of the year. We also increased resources in our Global Service Centres as we continued to move processes there.

Staff costs declined in the US due to the non-recurrence of restructuring costs associated with the closure of the Consumer Lending branch network in 2009. Also, headcount fell due to the sale of the vehicle finance portfolio and related servicing platform. Similarly, reported staff numbers fell in Europe due to the sale of the insurance broking business in the UK and business reorganisation in France, though this was partly offset by higher numbers of customer-facing staff in the UK and Turkey.

Premises and equipment costs increased as rental costs in the UK, the US and France rose following the sale and leaseback of 8 Canada Square, London and our headquarters buildings in the US and France, combined with business expansion in Asia and Europe and refurbishment costs in Europe and Latin America. This was partly offset by lower costs in the US following the closure of the Consumer Lending branch offices and the non-recurrence of the related restructuring costs.

General and administrative expenses rose, reflecting in part higher marketing and advertising costs. These grew in North America in Card and Retail Services, partly from complying with the CARD Act. Marketing costs also rose in Asia and Latin America in support of the launch of Advance and sales campaigns for credit cards and investment products. Project costs increased from various initiatives to enhance operational capabilities, in connection with which consultancy and contractors fees rose, primarily in the UK as GB&M continued to invest in strategic initiatives to drive future revenue growth. These included the development of Prime Services and equity market capabilities, and the expansion of the Rates and foreign exchange e-commerce platforms.

Travel costs increased as we increased our focus on international connectivity and business growth. Costs also increased due to litigation provisions in North America and Europe.

Cost efficiency ratios

	2010	2009	2008
	%	%	%
HSBC	**55.2**	52.0	60.1
Personal Financial Services	**57.7**	51.7	76.4
Europe	**67.4**	68.7	62.7
Hong Kong	**35.3**	34.9	32.2
Rest of Asia-Pacific	**85.1**	81.2	81.5
Middle East	**62.2**	53.5	53.2
North America	**46.9**	38.1	106.8
Latin America	**72.1**	66.7	59.7

Commercial Banking	**49.4**	46.4	43.0
Europe	**51.9**	47.4	44.2
Hong Kong	**32.2**	33.7	26.2
Rest of Asia-Pacific	**49.2**	47.0	45.9
Middle East	**36.4**	33.8	32.0
North America	**46.6**	47.7	46.1
Latin America	**65.7**	57.0	55.0
Global Banking and Markets	**49.9**	39.1	67.3
Global Private Banking	**65.8**	60.5	58.3

Our cost efficiency ratio worsened by 3.2 percentage points on a reported basis and by 8.4 percentage points to 55.8% on an underlying basis.

In PFS, there was a deterioration of 5.7 percentage points in the cost efficiency ratio. Operating expenses remained broadly unchanged as a rise in costs in

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Asia in support of business expansion was broadly offset by strict cost control across the Group and lower costs in the US. Revenue fell, largely in the run-off portfolio and in Card and Retail Services in North America.

In CMB, the cost efficiency ratio deteriorated by 2.9 percentage points as we continued to invest for future revenue growth in those markets that we see as central to international connectivity. Revenue grew in all regions, albeit at a slower pace, resulting in a deterioration in the cost efficiency ratio, with the exception of Hong Kong where strong revenue growth led to an improvement of 1.5 percentage points.

In GB&M, the cost efficiency ratio deteriorated by 12.1 percentage points reflecting the one-off payroll and bonus taxes in the UK and France. Excluding them, the ratio deteriorated by 10.5 percentage points following a rise in costs related to higher support costs and continued investment in strategic initiatives being undertaken to drive future revenue growth. Revenue fell during 2010 mainly due to lower net interest income in Balance Sheet Management and lower trading income.

In GPB, the cost efficiency ratio deteriorated by 5.3 percentage points as costs increased, reflecting the hiring of front-line staff, investment in systems and higher compliance costs coupled with lower revenue in the low interest rate environment.

Share of profit in associates and joint ventures

	2010 US$m	2009 US$m	2008 US$m
Associates			
Bank of Communications Co., Limited	**987**	754	741
Ping An Insurance (Group) Company of China, Limited	**848**	551	324
Industrial Bank Co., Limited	**327**	216	221
The Saudi British Bank	**161**	172	251
Other	**156**	42	63
Share of profit in associates	**2,479**	1,735	1,600
Share of profit in joint ventures	**38**	46	61
Share of profit in associates and joint ventures	**2,517**	1,781	1,661

The share of profit from associates and joint ventures increased by 41% to US$2.5bn on both a reported and an underlying basis as our associates in mainland China capitalised on the improved economic conditions in region.

Our share of profits in Ping An Insurance increased due to strong insurance sales performance, while fee income and lending growth resulted in
higher profits from the Bank of Communications Co., Limited (Bank of Communciations) and from Industrial Bank Co., Limited (Industrial Bank).

These results were partly offset by a decrease in our share of profits from The Saudi British Bank as revenue declined amidst challenging economic conditions.

Tax expense

	2010	2009	2008
	US$m	US$m	US$m
Profit before tax	**19,037**	7,079	9,307
Tax expense	**(4,846)**	(385)	(2,809)
Profit after tax	**14,191**	6,694	6,498
Effective tax rate	**25.5%**	5.4%	30.2%

The most significant factor influencing the year on year changes to the effective tax rate is the changing geographical split of profits, including the relative proportion of tax on the share of profits in associates and joint ventures included within profit before tax. The impact of the tax on profit on associates and joint ventures included within pre-tax profits was a reduction in the effective tax rate of 3.7% in 2010 and 7.1% in 2009.

In 2010 HSBC s US operations achieved taxable profits, principally as a result of realising a taxable gain from an internal reorganisation which increased the effective tax rate by 6.4%. If this was excluded the effective tax rate would be 19.1% which is in line with the geographic profile of the Group.

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2009 compared with 2008
Reconciliation of reported and underlying profit before tax

	2009 compared with 2008								
HSBC	2008 as reported US$m	2008 adjust-ments[10] US$m	Currency translation[11] US$m	2008 at 2009 exchange rates[16] US$m	2009 as reported US$m	2009 adjust-ments[10] US$m	2009 under-lying US$m	Re-ported change[13] %	Under-lying change[13] %
Net interest income	42,563	(65)	(2,062)	40,436	40,730	(53)	40,677	(4)	1
Net fee income	20,024	(58)	(1,315)	18,651	17,664	(6)	17,658	(12)	(5)
Changes in fair value[14]	6,570	(6,570)			(6,533)	6,533			
Gains on disposal of French regional banks	2,445	(2,445)						(100)	
Other income	10,080	(680)	(1,597)	7,803	14,320	(298)	14,022	42	80
Net operating income[15]	81,682	(9,818)	(4,974)	66,890	66,181	6,176	72,357	(19)	8
Loan impairment charges and other credit risk provisions	(24,937)	6	709	(24,222)	(26,488)		(26,488)	(6)	(9)
Net operating income	56,745	(9,812)	(4,265)	42,668	39,693	6,176	45,869	(30)	8
Operating expenses (excluding goodwill impairment)	(38,535)	68	2,655	(35,812)	(34,395)	31	(34,364)	11	4
Goodwill impairment	(10,564)			(10,564)				100	100

Operating profit	7,646	(9,744)	(1,610)	(3,708)	5,298	6,207	11,505	(31)	
Income from associates	1,661		25	1,686	1,781		1,781	7	6
Profit before tax	9,307	(9,744)	(1,585)	(2,022)	7,079	6,207	13,286	(24)	
By geographical region									
Europe	10,869	(6,221)	(1,054)	3,594	4,009	2,561	6,570	(63)	83
Hong Kong	5,461	(5)	20	5,476	5,029	1	5,030	(8)	(8)
Rest of Asia-Pacific	4,722	(3)	(184)	4,535	4,200	(43)	4,157	(11)	(8)
Middle East	1,746		(7)	1,739	455		455	(74)	(74)
North America	(15,528)	(3,444)	(67)	(19,039)	(7,738)	3,688	(4,050)	50	79
Latin America	2,037	(71)	(293)	1,673	1,124		1,124	(45)	(33)
Profit before tax	9,307	(9,744)	(1,585)	(2,022)	7,079	6,207	13,286	(24)	
By customer group and global business									
Personal Financial Services	(10,974)	(148)	(457)	(11,579)	(2,065)	(3)	(2,068)	81	82
Commercial Banking	7,194	(486)	(665)	6,043	4,275	(318)	3,957	(41)	(35)
Global Banking and Markets	3,483		(479)	3,004	10,481	(5)	10,476	201	249
Global Private Banking	1,447		(48)	1,399	1,108		1,108	(23)	(21)
Other	8,157	(9,110)	64	(889)	(6,720)	6,533	(187)		79
Profit before tax	9,307	(9,744)	(1,585)	(2,022)	7,079	6,207	13,286	(24)	

Consolidated income statement

Our reported pre-tax profits in 2009 fell by 24% to US$7.1bn and earnings per share declined to US$0.34. Return on average shareholders equity remained broadly at 2008 levels at 5.1% (2008: 4.7%).

On an underlying basis, our profit before tax increased by US$15.3bn compared with 2008. The difference between reported and underlying results is explained on page 14. Except where otherwise stated, the commentaries in the Financial Summary are on an underlying basis.

Profit before tax on an underlying basis and excluding the goodwill impairment charge of US$10.6bn in 2008, was 56% or US$4.7bn higher.

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The increase in profit before tax was driven by strong growth in net operating income in GB&M, in part reflecting the absence of significant write-downs in securities and structured credit positions which had affected results in 2008. More significantly, the business benefited from market share gains in core activities and the effect of early positioning by Balance Sheet Management, in anticipation of the low interest rate environment. Results in 2009 also reflected lower loan impairment charges in North America, partly offset by an increase in loan impairment charges and other credit risk provisions elsewhere.

Although our business in North America continued to record a loss, performance improved as write-downs in GB&M reduced and loan impairment charges in PFS decreased. This resulted from steps taken to curtail origination in 2007 and 2008, which culminated in the closure of the Consumer Lending branch network in the second quarter of 2009, and from our decision to place all consumer finance portfolios other than credit cards into run-off. The closure of the branch network fed through to lower operating expenses during the remainder of the year.

In Hong Kong, economic performance remained robust despite continuing challenges, with our results underpinned by a market-leading share in deposits, residential mortgages, cards and insurance. Overall profitability declined, however, as revenue was driven lower by compressed deposit spreads in the low interest rate environment. Loan impairment charges improved on 2008, remaining low, and operating expenses reflected a disciplined approach to cost management.

In the Rest of Asia-Pacific region, the economic challenges faced were similar to those in Hong Kong and their impact was reflected in lower income and higher loan impairment charges. Income from associates, primarily in mainland China, made a significant positive contribution to the region s performance. We continued to expand our presence in Rest of Asia-Pacific through organic growth and strategic investment.

Our Middle East operations suffered from a combination of factors: a severe contraction in the economy of Dubai, a fall in oil revenues for much of the year and investment losses incurred by many regional investors. This led to a decline in profit before tax of 74%, primarily due to a significant increase in loan impairment charges. The regional economic downturn and continuing uncertainty affected both retail and corporate customers, particularly in the United Arab Emirates (UAE) where the downturn was most pronounced.

In Europe, we reported an increase in profit before tax on an underlying basis, driven by GB&M in London and Paris. This resulted from a strong performance in Rates and Balance Sheet Management, coupled with the benefit of stabilisation of asset prices and general tightening of credit spreads and lower write-downs in the credit trading business. This was partly offset by a reduction in deposit spreads in PFS and CMB as interest rates fell, and an increase in loan impairment charges in Global Banking, reflecting a deterioration in the credit position of a small number of clients.

The increase in profit before tax was driven by strong growth in GB&M.

In Latin America, the decline in pre-tax profits was driven by an increase in loan impairment charges in PFS and CMB and lower revenues in PFS, partly offset by a strong performance in trading and Balance Sheet Management in GB&M. The lower revenues in PFS were in part due to the continued curtailment of personal unsecured credit exposures, following our adverse experience in 2008, with net interest income also adversely affected by declining interest rates and narrowing spreads.

With the exception of PFS, which continued to be heavily affected by the consumer finance losses in North America, all customer groups remained profitable.

The following items are significant to a comparison of reported results with 2008:

the non-recurrence of the US$10.6bn goodwill impairment charge in North America recorded in 2008;

the non-recurrence of a US$2.4bn gain on the sale of French regional banks in 2008;

fair value losses relating to own credit spreads of US$6.5bn in 2009 compared with gains of US$6.6bn in 2008;

a US$72m fraud loss relating to Bernard L Madoff Investment Securities LLC (Madoff Securities) in 2009, which was in addition to the US$984m charge reported in 2008;

loss from write-downs in legacy securities and structured credit positions amounting to US$0.3bn in 2009 compared with US$5.4bn in 2008;

the acquisition in 2008 of the subsidiary, Project Maple II B.V., which owned our headquarters at 8 Canada Square, London E14 5HQ and the subsequent sale of the company and leaseback of the property in 2009, resulting in gains of US$0.6bn in 2009 and US$0.4bn in 2008;

the sale of the card merchant-acquiring business in the UK, resulting in gains of US$0.3bn in 2009 and US$0.4bn in 2008;

the change in the basis of delivering long-term employee benefits in the UK, which generated a one-off accounting gain of US$0.5bn in 2009; and

the tax expense of US$0.3bn in 2009, which was lower than in previous years as a result of the geographic distribution of income. We generated profits in low tax rate jurisdictions, principally Asia, and incurred losses in high tax rate jurisdictions, principally the US, which when mixed produced a low overall rate.

Group performance by income and expense item

Net interest income

Our reported net interest income of US$40.7bn fell by 4% compared with 2008, but was marginally higher on an underlying basis.

Reported net interest income includes the expense of the internal funding of trading assets, while related revenue is reported in trading income. The cost of internally funding these assets declined significantly as a result of the low interest rate environment. In our customer group reporting, this cost is included within trading income.

Deposit spreads were squeezed by the exceptionally low interest rates, although this was partly offset by the reduced cost of funding trading activities. Strong revenues in Balance Sheet Management reflected positions taken in 2008 ahead of the reduction in major currency interest rates. As these positions began to mature, the revenue from Balance Sheet Management s activities reduced but remained strong in the second half of 2009.

Average interest-earning assets fell slightly due to a decline in term lending, mainly from the run-off portfolios in North America and the decline in consumer credit appetite globally.

Average interest-bearing liabilities also decreased, due to a decline in debt securities in issue as funding requirements for HSBC Finance fell as certain portfolios were managed down. This was largely offset by a rise in current account balances, driven by growth in customer demand for more liquid assets. The very low interest rates led to clients holding an increasing proportion of funds in liquid current accounts rather than in savings and deposit accounts as they positioned for rising interest rates or prospective investment opportunities.

Competition for deposits and exceptionally low interest rates squeezed deposit margins.

The net interest spread rose slightly. As a result of continuing deposit inflows, we sourced an increasing proportion of our funding from customer accounts, and consequently reduced our reliance on relatively more expensive debt securities. The benefit of this was largely offset, however, by a decline in customer lending, particularly higher yielding personal lending, which reduced the average yield on assets.

Net fee income

Reported net fee income decreased by 12% to US$17.7bn, 5% lower on an underlying basis.

Lower credit card fees and weaker equity markets led to a decline in net fee income.

Credit card fees fell significantly, mainly in North America, reflecting lower transaction volumes, a reduction in cards in issue and changes in customer behaviour which led to lower cash advance, interchange, late and overlimit fees. In the UK, the decrease primarily arose from the disposal of the card-acquiring business to a joint venture in June 2008.

Weaker equity markets and subdued investor sentiment for higher risk products led to a reduction in both the volume and the value of equity-related products. This resulted in a decrease in fees generated from funds under management, global custody and unit trusts, though fees grew from equity capital markets products in GB&M. The impact was particularly marked in the first half of 2009, though market-related fees recovered somewhat in the second half of the year as market values rose and investor appetite for equity products increased.

Account services fees fell, predominantly in North America as the result of a decline in credit card volumes and changes in customer behaviour, and in GPB due to a decrease in fiduciary deposit commissions as lower interest rates drove down balances.

Insurance broking fees also fell, mainly due to lower origination volumes of credit-related products, principally in the US consumer finance business, and reduced payment protection business in the UK.

Corporate credit facility and underwriting fees increased strongly on the back of higher debt originations in Europe and North America which accompanied the considerable reconstruction and refinancing of corporate balance sheets in 2009.

Net trading income

Reported net trading income increased by 50% to US$9.9bn, 83% higher on an underlying basis.

Reported trading income excludes the interest expense of the internal funding of trading assets. As noted in Net interest income , the cost of internally funding these assets declined significantly as a result of the low interest rate environment.

The Credit business benefited from a general tightening of credit spreads following a return of liquidity to much of the market, and the write-downs on legacy positions in Credit trading declined significantly following the stabilisation of asset prices.

Net trading income rose by 83% on an underlying basis.

An increase in Rates revenues, particularly in the first half of the year, reflected increased market share and client trading volumes, wider bid-offer spreads and early positioning for interest rate movements. Partly offsetting these gains, fair value losses were recorded on our structured liabilities as a result of credit spreads tightening, compared with gains in this area in 2008.

Equities benefited from the non-recurrence of the US$984m charge reported in 2008 in respect of Madoff Securities. The core Equities business also took advantage of a changed competitive landscape to capture a greater share of business in strategic markets from key institutional clients.

Foreign exchange trading revenues were well ahead of 2007, but fell short of the record year in 2008. This reflected a combination of reduced customer volumes from lower trade flows and investment activity, and relatively lower market volatility.

Tightening credit spreads led to losses of US$429m on credit default swap transactions in parts of the Global Banking portfolio. In 2008, gains of US$912m were reported on these credit default swaps as a result of widening credit spreads.

A reduction in net interest income on trading activities reflected the sharp fall in interest rates at the end of 2008 but was partly compensated for by a reduction in the internal funding cost of trading activities, which is reported in Net interest income .

Income from non-qualifying hedges related to mark-to-market gains on cross-currency swaps as the US dollar depreciated against sterling, and on interest rate swaps as US dollar long and medium term interest rates increased over the year. In 2008, appreciation of the US dollar and a fall in interest rates led to mark-to-market losses on these instruments.

During the second half of 2008, we reclassified US$17.9bn of assets from held for trading to loans and receivables and available for sale following the IASB s amendment to International Accounting Standard (IAS) 39. Had these reclassifications not taken place and the assets had continued to be accounted for on a fair value basis, we would have recorded additional gains of US$1.5bn in 2009 (2008: losses of US$3.5bn).

Net income from financial instruments designated at fair value

We designate certain financial instruments at fair value to remove or reduce accounting mismatches in measurement or recognition, or where financial instruments are managed and their performance is evaluated together on a fair value basis. All income and expense from financial instruments designated at fair value are included in this line except for interest arising from our issued debt securities and related derivatives managed in conjunction with those debt securities, which is recognised in Interest expense .

We principally use the fair value designation in the following instances (for which all numbers are reported):

for certain fixed-rate long-term debt issues whose rate profile has been changed to floating through interest rate swaps as part of a documented interest rate management strategy. Approximately US$63bn (2008: US$59bn) of our debt issues have been accounted for using the fair value option.

The movement in fair value of these debt issues includes the effect of own credit spread changes and any ineffectiveness in the economic relationship between the related swaps and own debt. As credit spreads widen or narrow, accounting profits or losses, respectively, are booked. The size and direction of the accounting consequences of changes in own credit spread and ineffectiveness can be volatile from year to year, but do not alter the cash flows envisaged as part of the documented interest rate management strategy. As a consequence, gains and losses arising from changes in own credit spread on long-term debt are not regarded internally as part of managed performance and are excluded from underlying results. Similarly, such gains and losses are ignored in the calculation of regulatory capital;

for US$15bn (2008: US$11bn) of financial assets held to meet liabilities under insurance contracts, and certain liabilities under investment contracts with discretionary participation features; and

for US$8bn (2008: US$7bn) of financial assets held to meet liabilities under unit-linked and other investment contracts, as well as the associated liabilities.

A net expense from financial instruments designated at fair value of US$3.5bn was reported compared with income of US$3.9bn in 2008.

A significant change in credit spread on our own debt in 2009 reversed the movement in 2008.

On an underlying basis, we reported income of US$3.0bn in 2009 compared with an expense of US$2.6bn in 2008. The large difference between the reported and underlying results is due to the exclusion of the effect of credit spread-related movements in the fair value of our own long-term debt from underlying performance.

Income of US$3.8bn was recorded due to a fair value movement on assets held to back insurance and investment contracts, compared with an expense of US$4.8bn in 2008. This reflected investment gains in the current year driven by improved market performance, predominantly affecting the value of assets held in unit-linked and participating funds in Hong Kong, the UK and France.

To the extent that the investment gains related to assets held to back investment contracts, the expense associated with the corresponding increase in liabilities to customers was also recorded under net income from financial instruments designated at fair value. This expense amounted to US$1.3bn in 2009 compared with an income of US$1.5bn in 2008 when liabilities fell in line with declining asset markets.

To the extent that the investment gains related to assets held to back insurance contracts, they were offset by a corresponding increase in Net insurance claims and movement in liabilities to policyholders to reflect the extent to which unit-linked policyholders, in particular, participate in the investment performance experienced in the associated asset portfolios.

Gains less losses from financial investments

Reported gains less losses from financial investments increased by US$323m to US$520m. On an underlying basis, they increased by US$546m.

Net gains on the disposal of debt securities increased significantly, due to gains recorded on the sale of mortgage-backed securities in North America. They were supplemented by smaller gains, principally on the disposal of available-for-sale bonds in Latin America and the UK.

Sales of Visa shares contributed significant gains during 2008, with additional gains from further sales in 2009. Other gains recognised during 2008, including those recorded on the sale of MasterCard shares, were not repeated in 2009.

A significantly lower level of impairments on equity investments was recognised in 2009 than in 2008 in Asia, Europe and North America, reflecting the improvement in the economic situation and equity markets. Of the investments on which material impairments were recognised in 2008, a significant amount reversed during 2009 due to share price appreciation, notably in India and, to a lesser extent, Vietnam; however, under IFRSs all subsequent increases in the fair value are treated as a revaluation and are recognised in other comprehensive income rather than the income statement.

Net earned insurance premiums

Reported net earned insurance premiums amounted to US$10.5bn, a decrease of 3% compared with 2008. On an underlying basis, net earned insurance premiums increased by 3%. Growth was recorded in Asia, Brazil and France, but this was largely offset by significant declines in the UK and the US.

Net earned insurance premiums continued to grow in Asia, mainly from the launch of new products including a life insurance product designed for high net worth individuals and a guaranteed savings product. In Hong Kong, we retained our position as the leading bancassurer and increased net earned insurance premiums as a result of higher sales of unit-linked and whole life products.

Growth in insurance premiums in Asia, Brazil and France was largely offset by declines in the UK and US.

In Latin America, premium growth was driven by higher sales of pension and life products in Brazil, partly due to a number of customers switching their personal pension annuities to us.

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In France, growth was significantly influenced by a large one-off reinsurance transaction in June 2008, which passed insurance premiums to a third-party reinsurance provider. Adjusting for this, net earned insurance premiums were ahead of 2008 despite a significant reduction in the distribution network following the disposal of the French regional banks in July 2008.

In the UK, demand for the Guaranteed Income Bond savings product declined as HSBC offered more favourable rates on an alternative deposit product. As the deposit product was a savings bond rather than an insurance contract, its income was recorded under net interest income, while the associated fall in sales of insurance products led to a US$1.1bn reduction in insurance premium income with an equivalent decrease in Net insurance claims incurred and movement in liabilities to policyholders , as described below.

The reduction in origination volumes in the consumer finance business in North America also led to correspondingly lower sales of credit protection insurance as the consumer finance business was closed.

Other operating income

Reported other operating income of US$2.8bn was 54% higher than in 2008. This included a US$280m gain related to the sale of the remaining stake in the card merchant-acquiring business in the UK, compared with a US$425m gain in 2008 from the sale of the first tranche. In 2008, results also included gains of US$71m related to the sale of our stake in Financiera Independencia. On an underlying basis, other operating income rose by 163%, driven mainly by an increase in insurance-related income in Hong Kong, a rise in gains on property disposals and lower losses on foreclosed properties.

Increased insurance income in Hong Kong, higher gains on property disposals and lower losses on foreclosed properties in the US helped drive an underlying US$1.5bn rise in other operating income.

Losses recognised on assets held for sale declined as losses on foreclosed properties in HSBC Finance decreased, partly due to lower inventory levels following delays in the foreclosure process and partly due to some stabilisation in real estate prices.

Property gains of US$576m were recognised in respect of the sale and leaseback of 8 Canada Square, London which was effected through the disposal of our entire shareholding in Project Maple II B.V. (PMII) to the National Pension Service of Korea.

In 2008, we reported a gain of US$416m in respect of the purchase of PMII.

An increase in insurance sales to new customers in Hong Kong resulted in positive movements in the present value of in-force (PVIF) long-term insurance business. Further positive movements arose from refining the income recognition methodology used in respect of long-term insurance contracts in HSBC Finance. In 2008, a similar refinement in Brazil and our introduction of enhanced benefits to existing pension products in the UK, resulted in favourable movements in PVIF.

In Hong Kong, a gain of US$110m was recognised in respect of a property disposal, and in Argentina a gain was realised on the sale of the head office building.

Other operating income includes higher gains on the sale of prime residential mortgage portfolios in the US, gains from the extinguishment of certain debt issued by our mortgage securitisation vehicles in the UK and lower costs associated with the provision of support to certain money market funds.

Net insurance claims incurred and movement in liabilities to policyholders

Reported net insurance claims incurred and movement in liabilities to policyholders increased by 81% to US$12.5bn. On an underlying basis, they increased by 94%.

The increase in net insurance claims incurred and movement in liabilities to policyholders mainly reflected the improvement in investment market performance compared with 2008 described above under Financial instruments designated at fair value . Higher investment gains were broadly matched by movement in liabilities to policyholders on unit-linked and, to a certain extent, participating policies whose policyholders share in the investment performance of the supporting assets. The gains generated on the assets held to support insurance contract liabilities are reported in Net income from financial instruments designated at fair value .

New business growth in a number of regions during 2009, particularly Hong Kong and Singapore, also contributed to an increase in the movement in liabilities to policyholders, as did the non-recurrence of a large one-off reinsurance transaction in France in 2008. The decline in sales of a Guaranteed Income Bond noted above had a corresponding effect on movement in liabilities to policyholders in the UK.

As a consequence of a rising incidence and severity of claims, aggregate charges of US$310m were made to strengthen reserves in the UK motor book and the Irish reinsurance business during 2009. The UK motor insurance business was placed into run-off in September 2009.

Loan impairment charges and other credit risk provisions

Reported loan impairment charges and other credit risk provisions were US$26.5bn in 2009, an increase of 6% over 2008, 9% on an underlying basis. Within this, collectively assessed impairment allowances declined while individually assessed impairment allowances continued to increase.

Our aggregate outstanding customer loan impairment allowances at 31 December 2009 of US$25.5bn represented 3% of gross customer advances (net of reverse repos and settlement accounts) compared with 2.6% at the end of 2008.

Loan impairment charges declined in certain businesses, notably PFS in North America and CMB in Hong Kong, but this was more than offset by increases elsewhere, primarily on individually significant loans within GB&M and more broadly on CMB exposures outside Hong Kong as the global economic downturn adversely affected the ability of many customers to service their loan commitments. As a consequence, loan impairment charges rose despite an underlying 9% decline in gross loans and advances to customers which was driven mainly by the run-off of the US consumer finance portfolios.

In our US PFS business, loan impairment charges declined by 11% to US$14.2bn, as additional delinquencies due to the continued deterioration in the US economy were more than offset by the effect of lower balances in the run-off portfolios in HSBC Finance.

In HSBC Finance, loan impairment charges decreased by 12%. The reduction arose in most portfolios, but mainly in Mortgage Services as the portfolio continued to run off. In Consumer Lending, loan impairment charges increased, particularly in the unsecured personal lending portfolio, due to a deterioration in the 2006 and 2007 vintages and, to a lesser extent, first lien real estate secured loans, which was partly offset by lower loan impairment charges in the real estate secured portfolio. Loan impairment charges in the Card and Retail Services portfolio decreased despite the state of the US economy and higher levels of unemployment and personal bankruptcy. The main reason was the decline in card balances following actions taken to manage risk beginning in the fourth quarter of 2007 and continuing through 2009, and stable credit conditions.

In HSBC Bank USA, increased loan impairment charges in the personal lending portfolios were due to additional delinquencies which resulted in increased write-offs in the prime first lien mortgage loan portfolios as house prices continued to deteriorate in certain markets.

Loan impairment charges and other credit risk provisions increased significantly in GB&M. Loan impairment charges increased, reflecting the impairment of a small number of exposures in the financial and property sectors in Europe and the Middle East. Further impairments were also recognised in respect of certain asset-backed securities held in the available-for-sale portfolio, reflecting mark-to-market losses which we judged to be significantly in excess of the likely ultimate cash losses.

Loan impairment charges declined in PFS in the US but rose in CMB outside Hong Kong and in GB&M.

In the UK, loan impairment charges rose in both the CMB and PFS portfolios. However, despite the contraction in the economy, charges remained a low proportion of the portfolio. In CMB, loan impairment charges largely reflected economic weakness in a broad range of sectors.

In UK PFS, loan impairment charges also increased as unemployment rose. This was seen primarily in the credit card and unsecured personal loan portfolios. In the residential mortgage portfolios, delinquency rates decreased as we continued to benefit from very limited exposure to buy-to-let and self-certified mortgages. Our mortgage exposure continued to be well secured, with an average loan-to-value ratio for new UK business in HSBC Bank s mortgage portfolio, excluding First Direct, of under 55% in 2009, compared with 59% in 2008.

In the Middle East, our loan impairment charges increased markedly from US$280m to US$1.3bn as the region experienced a significant economic contraction in activity, predominantly in real estate and construction, which particularly affected the UAE. CMB recorded a number of specific loan impairment charges and a significant increase in collective loan impairment charges. Lower employment in the region, largely driven by the decline in construction activity, led to a rise in loan impairment charges in PFS, particularly in the credit card and personal lending portfolios.

In Latin America, our portfolios were affected by the weaker economic environment for much of the year. In PFS, loan impairment charges rose by 12% to US$2.0bn, with increased delinquencies in credit cards, mortgages, vehicle finance and payroll loans due to higher unemployment. In the Brazilian CMB portfolios, higher delinquencies were experienced primarily in the business banking and mid-market segments. In Mexico, action taken in 2008 to curtail originations and increase collection resources held loan impairment charges broadly unchanged notwithstanding the deterioration in the economy and the impact of the H1N1 virus.

In India, as in Mexico, curtailment of origination activity in unsecured personal lending slowed the increase in loan impairment charges in the unsecured credit card and personal lending portfolios in PFS. In CMB, a higher number of corporate failures including a number of fraud-related losses, led to increased loan impairment charges.

Loan impairment charges and other credit risk provisions in Hong Kong decreased by 35% to US$500m as the economic environment improved in 2009, credit conditions recovered and international trade volumes improved.

In GPB, loan impairment charges increased from a very low level, largely attributable to a specific charge relating to a single client relationship in the US.

Operating expenses

Reported operating expenses fell by US$14.7bn to US$34.4bn, with the most significant feature being the non-recurrence of the goodwill impairment charge of US$10.6bn in 2008 to fully write off goodwill in PFS in North America. Excluding this and on an underlying basis, operating expenses fell by 4%.

Underlying operating expenses excluding goodwill impairment fell by 4%.

Employee compensation and benefits fell by 4% as costs in the US declined following the closure of the branch-based consumer finance business in the first quarter of 2009. Average headcount in most regions was lower and this was reflected in lower costs. In the UK, a change in the basis of delivering death-in-service, ill health and early retirement benefits for some UK employees generated a one-off accounting gain of US$499m which was partly offset by increased regular pension costs. There were higher performance-related costs in GB&M reflecting its results. The UK and French governments announced one-off taxes in late 2009 in respect of certain bonuses payable by banks and banking groups. In both countries there is uncertainty over the interpretation of the draft proposals, and detailed analysis of individual awards
in the context of the final legislation will be required to determine the precise effect of the taxes. The estimated tax payable under the proposals as currently drafted is US$355m in the UK and US$45m in France. The taxes will be payable and accounted for in 2010 once the legislation is enacted.

Premises and equipment costs increased marginally with higher rental costs reflecting the sale and leaseback of a number of properties in 2008. One-off costs incurred due to the closure of the Consumer Lending branch network in the US were partly offset by savings resulting from the closure.

General and administrative expenses fell as we focused on managing costs tightly and increasing efficiency. Marketing and advertising costs fell across the Group, most notably in Card and Retail Services in North America, and in the UK. Travel and entertainment costs, and expenditure related to services contracted to third parties, fell, primarily in Europe and North America. Better use of direct channels, increased automation of manual processes, enhanced utilisation of global service centres and elimination of redundant systems continued to be driven through our One HSBC programme. In North America, cost savings also resulted in the Consumer Lending Business from the discontinuation of loan originations and the closure of branches.

Share of profit in associates and joint ventures

The share of profit in associates and joint ventures was US$1.8bn, an increase of 7% on 2008, and 6% on an underlying basis.

Our share of profits from Ping An Insurance increased by 62% as a result of the non-recurrence of its impairment of its investment in Fortis SA/NV and Fortis N.V. (Fortis) in 2008 and an increase in new business sales and investment returns which were boosted by a recovery in equity markets during 2009. This was partly offset by the non-recurrence of favourable changes to investment assumptions in the first half of 2008.

6% underlying increase in share of profit in associates and joint ventures.

Our share of profits from the Bank of Communications remained in line with 2008 as higher fee and trading income and a lower tax charge were broadly offset by a decline in net interest income and higher loan impairment charges.

Profits from The Saudi British Bank were lower than in 2008 as an increase in loan impairment charges was only partly offset by increased operating income.

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The share of profits from joint ventures fell due to a decline in the profitability of HSBC Saudi Arabia Ltd as a result of a slowdown in initial public offerings (IPO s) and a decline in assets under management. This was partly offset by an increase in profits from HSBC Merchant Services UK Ltd in the first half of 2009 compared with the second half of 2008. HSBC Merchant Services UK Ltd was created in June 2008 and sold in June 2009.

Tax expense

The most significant factor influencing the year on year changes to the effective tax rate is the changing geographical split of profits, including the relative proportion of tax on the share of profits in associates and joint ventures included within profit before tax. The impact of the tax on profit on associates and joint ventures included within pre-tax profits was a reduction in the effective tax rate of 7.1% in 2009 and 5.1% in 2008.

In 2009 the losses in HSBC s US operations were tax effected at the local tax rate of 35.4%, while the profits in the rest of the HSBC Group were taxed at their local rates which averaged 18.8%. The combination of these two rates produced an overall tax effect of 5.44%.

The tax expense and effective tax rate also fell in 2009 due to the non-recurrence of the US$10.6bn goodwill impairment charge in North America which, for tax purposes, was non-deductible and hence increased the effective tax rate by some 16% in 2008.

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Consolidated balance sheet

Five-year summary consolidated balance sheet and selected financial information

	At 31 December				
	2010	2009	2008	2007	2006
	US$m	US$m	US$m	US$m	US$m
ASSETS					
Cash and balances at central banks	**57,383**	60,655	52,396	21,765	12,732
Trading assets	**385,052**	421,381	427,329	445,968	328,147
Financial assets designated at fair value	**37,011**	37,181	28,533	41,564	20,573
Derivatives	**260,757**	250,886	494,876	187,854	103,702
Loans and advances to banks	**208,271**	179,781	153,766	237,366	185,205
Loans and advances to customers[35]	**958,366**	896,231	932,868	981,548	868,133
Financial investments	**400,755**	369,158	300,235	283,000	204,806
Other assets	**147,094**	149,179	137,462	155,201	137,460
Total assets	**2,454,689**	2,364,452	2,527,465	2,354,266	1,860,758
LIABILITIES AND EQUITY					
Liabilities					
Deposits by banks	**110,584**	124,872	130,084	132,181	99,694
Customer accounts	**1,227,725**	1,159,034	1,115,327	1,096,140	896,834
Trading liabilities	**300,703**	268,130	247,652	314,580	226,608
Financial liabilities designated at fair value	**88,133**	80,092	74,587	89,939	70,211
Derivatives	**258,665**	247,646	487,060	183,393	101,478
Debt securities in issue	**145,401**	146,896	179,693	246,579	230,325
Liabilities under insurance contracts	**58,609**	53,707	43,683	42,606	17,670
Other liabilities	**109,954**	148,414	149,150	113,432	103,010
Total liabilities	**2,299,774**	2,228,791	2,427,236	2,218,850	1,745,830
Equity					
Total shareholders equity	**147,667**	128,299	93,591	128,160	108,352
Non-controlling interests	**7,248**	7,362	6,638	7,256	6,576
Total equity	**154,915**	135,661	100,229	135,416	114,928

Total equity and liabilities	**2,454,689**	2,364,452	2,527,465	2,354,266	1,860,758
Five-year selected financial information					
Called up share capital	**8,843**	8,705	6,053	5,915	5,786
Capital resources[36,37]	**167,555**	155,729	131,460	152,640	127,074
Undated subordinated loan capital	**2,781**	2,785	2,843	2,922	3,219
Preferred securities and dated subordinated loan capital[38]	**54,421**	52,126	50,307	49,472	42,642
Risk weighted assets and capital ratios[36]					
Risk weighted assets	**1,103,113**	1,133,168	1,147,974	1,123,782	938,678
	%	%	%	%	%
Tier 1 ratio	**12.1**	10.8	8.3	9.3	9.4
Total capital ratio	**15.2**	13.7	11.4	13.6	13.5
Financial statistics					
Loans and advances to customers as a percentage of customer accounts	**78.1**	77.3	83.6	89.5	96.8
Average total shareholders equity to average total assets	**5.53**	4.72	4.87	5.69	5.97
Net asset value per ordinary share at year-end[39] (US$)	**7.94**	7.17	7.44	10.72	9.24
Number of US$0.50 ordinary shares in issue (millions)	**17,686**	17,408	12,105	11,829	11,572
Closing foreign exchange translation rates to US$:					
US$1: £	**0.644**	0.616	0.686	0.498	0.509
US$1:	**0.748**	0.694	0.717	0.679	0.759

For footnotes, see page 83.

A more detailed consolidated balance sheet is contained in the Financial Statements on page 240.

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Movement in 2010

Total assets amounted to US$2.5 trillion, 4% higher than at 31 December 2009. Excluding the effect of currency movements, underlying total assets increased by 5%. This reflected higher mortgage lending in Hong Kong and the UK, strong demand for commercial loans and a rise in trading assets in North America and Asia as a result of customer demand, supported by improved liquidity generated by higher deposits and our debt issuance programme.

The Group s reported tier 1 ratio increased from 10.8% to 12.1% due to the contribution from profits attributable to shareholders for the year net of dividends paid, the issue of hybrid capital securities net of redemptions, and a reduction in the reported level of risk-weighted assets (RWA s). The latter was driven by a decline in some retail portfolio exposures in North America as a result of run-off, partly offset by the effect of lending growth in Asia. Market risk RWAs decreased as a result of reduced volatility and continuing exposure management. For more details of capital and RWAs, see page 177.

The following commentary is on an underlying basis.

Assets

Cash and balances at central banks decreased by 4% as a result of lower year-end cash balances in North America as excess liquidity was redeployed into highly-rated government debt securities. This was partly offset by higher year-end cash balances in Europe.

Trading assets fell by 6%, due to the deconsolidation of the Constant Net Asset Value (CNAV) funds totalling US$44bn (see Note 43 on the Financial Statements). This was offset, in part, by higher issuance of and customer demand for government and government agency debt securities, particularly in North America and Asia, and an increase in holdings of equities to hedge derivative positions arising from a rise in client trading activity. Higher customer-driven trading volumes also resulted in an increase in reverse repo balances in North America; this was partly offset by a reduction in reverse repo balances in Europe due to market uncertainty.

Strong increase in loans and advances to customers and customer accounts, notably in Asia, drove balance sheet growth.

Financial assets designated at fair value grew by 3% due to an increase in volumes in equity funds and a rise in the fair value of equity securities held
within the insurance business, particularly in Europe and Hong Kong, as market values recovered and client risk appetite returned. This was partly offset by the sale of European government debt securities by Balance Sheet Management.

Derivative assets rose by 8%. This was driven by increases in the fair value of interest rate contracts as a result of downward shifts of major yield curves, offset by higher netting from increased trading with clearing houses. The notional value of outstanding contracts also rose, reflecting an increase in the number of open transactions compared with 2009.

Loans and advances to banks increased by 16% due to higher placements with commercial and central banks in Europe and Latin America.

Loans and advances to customers grew by 8% as we targeted commercial loans and, in the improved economic conditions, demand grew from customers, notably in Asia. The increase in demand for credit, along with competitive pricing, also drove continued growth in mortgage lending in Hong Kong and the UK, though mortgage balances declined in North America as the Consumer Lending and Mortgage Services portfolios continued to run off and credit card lending fell.

Financial investments rose by 9%, mainly in North America and Europe, as Balance Sheet Management redeployed cash into available-for-sale treasury bills and government agency debt securities. This was partly offset by a decline in financial investments in Asia, as a result of disposals and debt securities that matured and were not replaced to support growth in commercial lending.

Liabilities

Deposits by banks decreased by 8%, reflecting a notable decline in central bank deposits in Europe which was partly offset by an increase in central bank deposits in Asia.

Customer accounts were 7% higher, driven by an overall increase in savings and current accounts across most regions, particularly in Asia and Europe. Growth in Premier and online savings contributed to a significant increase in current account balances as customers responded well to targeted promotional campaigns.

Trading liabilities increased by 16%. Higher repo balances in North America were reported as a result of increased trading volumes of treasury and corporate bonds driven by market volatility in the bond market. In Europe, short bond and equity positions used to hedge derivative transactions increased, reflecting higher client demand.

Financial liabilities designated at fair value rose by 12% due to debt issuances by HSBC entities in Europe during 2010.

Derivative businesses are managed within market risk limits and, as a consequence, the increase in the value of *derivative liabilities* broadly matched that of derivative assets.

Debt securities in issue were in line with 2009, as new issuances of medium-term notes by HSBC entities in Europe during 2010 were offset by lower funding requirements in North America as the consumer finance portfolios in run-off declined.

Liabilities under insurance contracts grew by 12%. This was driven by strong life insurance sales in Hong Kong following the launch of several new products, and gains on unit-linked products as investment market values improved.

Other liabilities were 26% lower than at 31 December 2009 due to the deconsolidation of the CNAV funds (see Trading assets above).

Equity

Total shareholders equity increased by 17%, driven by profits generated during the year and the issue of Perpetual Subordinated Capital Securities, a form of tier 1 hybrid capital securities, in June 2010. In addition, the negative balance on the available-for-sale reserve declined from US$10.0bn at 31 December 2009 to US$4.1bn at 31 December 2010, largely reflecting improvements in the market value of assets.

Reconciliation of reported and underlying assets and liabilities

	31 December 2010 compared with 31 December 2009						
HSBC	**31 Dec 09 as reported US$m**	**Currency Translation40 US$m**	**31 Dec 09 at 31 Dec 10 exchange rates US$m**	**Under-lying change US$m**	**31 Dec 10 as reported US$m**	**Reported change %**	**Under-lying change %**
Cash and balances at central banks	**60,655**	**(731)**	**59,924**	**(2,541)**	**57,383**	**(5)**	**(4)**
Trading assets	**421,381**	**(12,483)**	**408,898**	**(23,846)**	**385,052**	**(9)**	**(6)**
Financial assets designated at fair value	**37,181**	**(1,134)**	**36,047**	**964**	**37,011**		**3**
Derivative assets	**250,886**	**(9,285)**	**241,601**	**19,156**	**260,757**	**4**	**8**
Loans and advances to banks	**179,781**	**(5)**	**179,776**	**28,495**	**208,271**	**16**	**16**
Loans and advances to customers	**896,231**	**(10,788)**	**885,443**	**72,923**	**958,366**	**7**	**8**
Financial investments	**369,158**	**(268)**	**368,890**	**31,865**	**400,755**	**9**	**9**
Other assets	**149,179**	**(1,826)**	**147,353**	**(259)**	**147,094**	**(1)**	

Total assets	**2,364,452**	**(36,520)**	**2,327,932**	**126,757**	**2,454,689**	**4**	**5**
Deposits by banks	**124,872**	**(4,182)**	**120,690**	**(10,106)**	**110,584**	**(11)**	**(8)**
Customer accounts	**1,159,034**	**(8,064)**	**1,150,970**	**76,755**	**1,227,725**	**6**	**7**
Trading liabilities	**268,130**	**(8,660)**	**259,470**	**41,233**	**300,703**	**12**	**16**
Financial liabilities designated at fair value	**80,092**	**(1,570)**	**78,522**	**9,611**	**88,133**	**10**	**12**
Derivative liabilities	**247,646**	**(9,262)**	**238,384**	**20,281**	**258,665**	**4**	**9**
Debt securities in issue	**146,896**	**(1,066)**	**145,830**	**(429)**	**145,401**	**(1)**	
Liabilities under insurance contracts	**53,707**	**(1,593)**	**52,114**	**6,495**	**58,609**	**9**	**12**
Other liabilities	**148,414**	**(431)**	**147,983**	**(38,029)**	**109,954**	**(26)**	**(26)**
Total liabilities	**2,228,791**	**(34,828)**	**2,193,963**	**105,811**	**2,299,774**	**3**	**5**
Total shareholders equity	**128,299**	**(1,679)**	**126,620**	**21,047**	**147,667**	**15**	**17**
Non-controlling interests	**7,362**	**(13)**	**7,349**	**(101)**	**7,248**	**(2)**	**(1)**
Total equity	**135,661**	**(1,692)**	**133,969**	**20,946**	**154,915**	**14**	**16**
Total equity and liabilities	**2,364,452**	**(36,520)**	**2,327,932**	**126,757**	**2,454,689**	**4**	**5**

For footnote, see page 83.

In 2010, the effect of acquisitions was not material.

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Reconciliation of reported and underlying loans and advances to customers and customer accounts by geographical region

	31 December 2010 compared with 31 December 2009						
	31 Dec 09 as reported US$m	Currency translation[11] US$m	31 Dec 09 at 31 Dec 10 exchange rates US$m	Under-lying change US$m	31 Dec 10 as reported US$m	Reported change %	Under-lying change %
Loans and advances to customers (net)							
Europe	439,481	(20,778)	418,703	17,096	435,799	(1)	4
Hong Kong	99,381	(92)	99,289	41,402	140,691	42	42
Rest of Asia-Pacific	80,043	5,802	85,845	22,886	108,731	36	27
Middle East	22,844	(139)	22,705	1,921	24,626	8	8
North America	206,853	2,562	209,415	(18,883)	190,532	(8)	(9)
Latin America	47,629	1,857	49,486	8,501	57,987	22	17
	896,231	(10,788)	885,443	72,923	958,366	7	8
Customer accounts							
Europe	495,019	(21,560)	473,459	18,104	491,563	(1)	4
Hong Kong	275,441	(474)	274,967	22,517	297,484	8	8
Rest of Asia-Pacific	133,999	8,938	142,937	15,218	158,155	18	11
Middle East	32,529	(320)	32,209	1,302	33,511	3	4
North America	149,157	2,259	151,416	7,070	158,486	6	5
Latin America	72,889	3,093	75,982	12,544	88,526	21	17
	1,159,034	(8,064)	1,150,970	76,755	1,227,725	6	7

Reconciliation of reported and underlying loans and advances to customers and customer accounts by customer groups and global businesses

	31 December 2010 compared with 31 December 2009						
	31 Dec 09 as	Currency	31 Dec 09 at 31 Dec 10 exchange	Under-lying	31 Dec 10 as	Reported	Under-lying

	reported	translation[11]	rates	change	reported	change	change
	US$m	US$m	US$m	US$m	US$m	%	%
Loans and advances to customers (net)							
Personal Financial Services	**399,460**	(2,176)	397,284	(6,327)	**390,957**	(2)	(2)
Commercial Banking	**199,674**	(1,493)	198,181	41,105	**239,286**	20	21
Global Banking and Markets	**256,956**	(6,622)	250,334	34,169	**284,503**	11	14
Global Private Banking	**37,031**	(431)	36,600	4,065	**40,665**	10	11
Other	**3,110**	(66)	3,044	(89)	**2,955**	(5)	(3)
	896,231	(10,788)	885,443	72,923	**958,366**	7	8
Customer accounts							
Personal Financial Services	**499,109**	(1,710)	497,399	27,785	**525,184**	5	6
Commercial Banking	**267,388**	(1,537)	265,851	20,156	**286,007**	7	8
Global Banking and Markets	**284,727**	(4,711)	280,016	28,437	**308,453**	8	10
Global Private Banking	**106,533**	(108)	106,425	705	**107,130**	1	1
Other	**1,277**	2	1,279	(328)	**951**	(26)	(26)
	1,159,034	(8,064)	1,150,970	76,755	**1,227,725**	6	7

For footnote, see page 83.

In 2010, the effect of acquisitions was not material.

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Average balance sheet

Average balance sheet and net interest income

Average balances and related interest are shown for the domestic operations of our principal commercial banks by geographical region. Other operations comprise the operations of our principal commerical banking and consumer finance entities outside their domestic markets and all other banking operations, including investment banking balances and transactions.

Average balances are based on daily averages for the principal areas of our banking activities with monthly or less frequent averages used elsewhere.

Balances and transactions with fellow subsidiaries are reported gross in the principal commercial banking and consumer finance entities within Other interest-earning assets and Other interest-bearing liabilities as appropriate and the elimination entries are included within Other operations in those two categories.

Net interest margin numbers are calculated by dividing net interest income as reported in the income statement by the average interest-earning assets from which interest income is reported within the Net interest income line of the income statement. Interest income and interest expense arising from trading assets and liabilities and the funding thereof is included within Net trading income in the income statement.

Assets

	2010			2009			2008		
	Average balance US$m	**Interest income US$m**	**Yield %**	Average balance US$m	Interest income US$m	Yield %	Average balance US$m	Interest income US$m	Yield %
Summary									
Total interest-earning assets (itemised below)	**1,472,294**	**58,345**	**3.96**	1,384,705	62,096	4.48	1,466,622	91,301	6.23
Trading assets[63]	**332,511**	**6,027**	**1.81**	357,504	7,614	2.13	428,539	16,742	3.91
Financial assets designated at fair value[64]	**52,692**	**1,033**	**1.96**	62,143	1,032	1.66	37,303	1,108	2.97
Impairment provisions	**(22,905)**			(26,308)			(20,360)		
Non-interest-earning assets	**664,308**			667,942			596,885		
Total assets and interest income	**2,498,900**	**65,405**	**2.62**	2,445,986	70,742	2.89	2,508,989	109,151	4.35
Short-term funds and loans and advances to banks									

Europe	HSBC Bank	**47,741**	**1,290**	**2.70**	38,455	1,379	3.59	46,703	2,187	4.68
	HSBC Private Banking Holdings (Suisse)	**2,603**	**15**	**0.58**	4,451	43	0.97	8,040	333	4.14
	HSBC France	**47,094**	**337**	**0.72**	37,239	440	1.18	35,801	1,495	4.18
Hong Kong	Hang Seng Bank	**14,884**	**222**	**1.49**	16,626	202	1.21	17,402	587	3.37
	The Hongkong and Shanghai Banking Corporation	**16,544**	**117**	**0.71**	27,903	182	0.65	47,244	1,344	2.84
Rest of Asia-Pacific	The Hongkong and Shanghai Banking Corporation	**30,288**	**464**	**1.53**	23,107	326	1.41	27,907	881	3.16
	HSBC Bank Malaysia	**5,113**	**126**	**2.46**	3,776	81	2.15	4,659	165	3.54
Middle East	HSBC Bank Middle East	**5,335**	**60**	**1.12**	4,312	52	1.21	6,028	188	3.12
North America	HSBC Bank USA	**28,653**	**103**	**0.36**	2,338	94	4.02	9,595	328	3.42
	HSBC Bank Canada	**3,823**	**16**	**0.42**	2,934	10	0.34	3,354	107	3.19
Latin America	HSBC Mexico	**3,238**	**129**	**3.98**	3,722	149	4.00	3,682	247	6.71
	Brazilian operations[65]	**16,102**	**1,525**	**9.47**	10,490	1,003	9.56	7,959	951	11.95
	HSBC Bank Panama	**959**	**8**	**0.83**	1,187	10	0.84	1,133	30	2.65
	HSBC Bank Argentina	**169**	**20**	**11.83**	256	29	11.33	612	43	7.03
Other operations		**14,196**	**123**	**0.87**	15,782	199	1.26	19,992	760	3.80
		236,742	**4,555**	**1.92**	192,578	4,199	2.18	240,111	9,646	4.02

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HSBC HOLDINGS PLC
Report of the Directors: Operating and Financial Review (continued)

		2010 Average balance US$m	Interest income US$m	Yield %	2009 Average balance US$m	Interest income US$m	Yield %	2008 Average balance US$m	Interest income US$m	Yield %
Loans and advances to customers										
Europe	HSBC Bank	**265,163**	**9,761**	**3.68**	276,602	10,898	3.94	288,214	18,587	6.45
	HSBC Private Banking Holdings (Suisse)	**11,987**	**191**	**1.59**	9,993	176	1.76	12,355	494	4.00
	HSBC France	**66,910**	**1,684**	**2.52**	71,048	1,932	2.72	73,455	3,604	4.91
	HSBC Finance	**2,251**	**198**	**8.80**	3,094	319	10.31	4,808	505	10.50
Hong Kong	Hang Seng Bank	**51,028**	**1,313**	**2.57**	42,619	1,194	2.80	42,304	1,589	3.76
	The Hongkong and Shanghai Banking Corporation	**65,226**	**1,755**	**2.69**	55,287	1,757	3.18	54,628	2,291	4.19
Rest of Asia-Pacific	The Hongkong and Shanghai Banking Corporation	**81,080**	**3,928**	**4.84**	66,262	3,668	5.54	77,741	5,163	6.64
	HSBC Bank Malaysia	**9,614**	**531**	**5.52**	8,113	455	5.61	8,407	553	6.58
Middle East	HSBC Bank Middle East	**21,193**	**1,303**	**6.15**	22,612	1,593	7.04	23,697	1,549	6.54
North America	HSBC Bank USA	**78,556**	**4,582**	**5.83**	98,422	5,541	5.63	93,088	5,758	6.19
	HSBC Finance	**78,105**	**7,741**	**9.91**	101,132	9,941	9.83	140,957	15,835	11.23
	HSBC Bank Canada	**46,360**	**1,643**	**3.54**	43,072	1,499	3.48	48,331	2,455	5.08
Latin America	HSBC Mexico	**12,309**	**1,571**	**12.76**	12,185	1,708	14.02	17,252	2,565	14.87
		23,366	**5,118**	**21.90**	18,704	4,494	24.03	19,642	4,879	24.84

	Brazilian operations[65]									
	HSBC Bank Panama	**9,348**	**815**	**8.72**	9,302	864	9.29	8,620	810	9.40
	HSBC Bank Argentina	**2,460**	**367**	**14.92**	1,940	357	18.40	2,136	378	17.70
Other operations		**33,543**	**1,685**	**5.02**	29,670	1,905	6.42	28,027	1,707	6.09
		858,499	**44,186**	**5.15**	870,057	48,301	5.55	943,662	68,722	7.28
Financial investments										
Europe	HSBC Bank	**85,206**	**1,725**	**2.02**	79,763	2,321	2.91	83,725	3,840	4.59
	HSBC Private Banking Holdings (Suisse)	**17,013**	**287**	**1.69**	15,602	363	2.33	12,018	553	4.60
	HSBC France	**4,017**	**102**	**2.54**	5,327	141	2.65	14,862	795	5.35
Hong Kong	Hang Seng Bank	**30,334**	**541**	**1.78**	24,594	630	2.56	24,031	1,063	4.42
	The Hongkong and Shanghai Banking Corporation	**65,256**	**477**	**0.73**	52,965	644	1.22	15,361	563	3.67
Rest of Asia-Pacific	The Hongkong and Shanghai Banking Corporation	**37,833**	**1,161**	**3.07**	34,056	1,039	3.05	31,992	1,507	4.71
	HSBC Bank Malaysia	**911**	**28**	**3.07**	1,218	37	3.04	937	36	3.84
Middle East	HSBC Bank Middle East	**8,086**	**126**	**1.56**	6,996	118	1.69	5,671	144	2.54
North America	HSBC Bank USA	**38,541**	**1,156**	**3.00**	27,253	969	3.56	25,089	1,232	4.91
	HSBC Finance	**2,834**	**116**	**4.09**	2,426	120	4.95	2,908	143	4.92
	HSBC Bank Canada	**14,310**	**257**	**1.80**	10,282	205	1.99	7,037	197	2.80
Latin America	HSBC Mexico	**7,177**	**388**	**5.41**	3,916	227	5.80	3,470	244	7.03
	Brazilian operations[65]	**9,564**	**1,089**	**11.39**	6,930	820	11.83	6,758	853	12.62
	HSBC Bank Panama	**996**	**38**	**3.82**	604	39	6.46	618	47	7.61

HSBC Bank Argentina	**370**	**58**	**15.68**	181	35	19.34	287	47	16.38
Other operations	**56,523**	**1,826**	**3.23**	50,767	1,717	3.38	29,632	1,354	4.57
	378,971	**9,375**	**2.47**	322,880	9,425	2.92	264,396	12,618	4.77

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HSBC HOLDINGS PLC
Report of the Directors: Operating and Financial Review (continued)

Assets (continued)

		2010 Average balance US$m	**2010** Interest income US$m	**2010** Yield %	2009 Average balance US$m	2009 Interest income US$m	2009 Yield %	2008 Average balance US$m	2008 Interest income US$m	2008 Yield %
Other interest-earning assets										
Europe	HSBC Bank	**14,255**	**100**	**0.70**	17,406	188	1.08	25,885	630	2.43
	HSBC Private Banking Holdings (Suisse)	**17,738**	**241**	**1.36**	21,450	360	1.68	21,189	875	4.13
	HSBC France	**9,954**	**93**	**0.93**	11,867	172	1.45	23,414	630	2.69
Hong Kong	Hang Seng Bank	**1,077**	**13**	**1.21**	2,618	32	1.22	1,629	48	2.95
	The Hongkong and Shanghai Banking Corporation	**27,112**	**260**	**0.96**	26,657	214	0.80	33,571	949	2.83
Rest of Asia-Pacific	The Hongkong and Shanghai Banking Corporation	**18,476**	**55**	**0.30**	19,917	106	0.53	24,492	352	1.44
	HSBC Bank Malaysia	**745**	**14**	**1.88**	407	6	1.47	212	7	3.30
Middle East	HSBC Bank Middle East	**1,272**	**46**	**3.62**	541	46	8.50	843	63	7.47
North America	HSBC Bank USA	**3,467**	**58**	**1.67**	3,327	71	2.13	3,091	188	6.08
		2,895	**7**	**0.24**	2,995	6	0.20	2,638	63	2.39

	HSBC Finance									
	HSBC Bank Canada	**1,287**	**20**	**1.55**	773	9	1.16	1,025	25	2.44
Latin America	HSBC Mexico	**158**	**9**	**5.70**	138			193	2	1.04
	Brazilian operations[65]	**1,170**	**80**	**6.84**	1,074	46	4.28	1,438	147	10.22
	HSBC Bank Panama	**1,234**	**12**	**0.97**	1,372	9	0.66	1,807	23	1.27
	HSBC Bank Argentina	**87**			51			58	1	1.72
Other operations		**(102,845)**	**(779)**		(111,403)	(1,094)		(123,032)	(3,688)	
		(1,918)	**229**	**(11.94)**	(810)	171	(21.11)	18,453	315	1.71
Total interest-earning assets										
Europe	HSBC Bank	**412,365**	**12,876**	**3.12**	412,226	14,786	3.59	444,527	25,244	5.68
	HSBC Private Banking Holdings (Suisse)	**49,341**	**734**	**1.49**	51,496	942	1.83	53,602	2,255	4.21
	HSBC France	**127,975**	**2,216**	**1.73**	125,481	2,685	2.14	147,532	6,524	4.42
	HSBC Finance	**2,251**	**198**	**8.80**	3,094	319	10.31	4,808	505	10.50
Hong Kong	Hang Seng Bank	**97,323**	**2,089**	**2.15**	86,457	2,058	2.38	85,366	3,287	3.85
	The Hongkong and Shanghai Banking Corporation	**174,138**	**2,609**	**1.50**	162,812	2,797	1.72	150,804	5,147	3.41
Rest of Asia-Pacific	The Hongkong and Shanghai Banking Corporation	**167,677**	**5,608**	**3.34**	143,342	5,139	3.59	162,132	7,903	4.87
	HSBC Bank Malaysia	**16,383**	**699**	**4.27**	13,514	579	4.28	14,215	761	5.35

Middle East	HSBC Bank Middle East	**35,886**	**1,535**	**4.28**	34,461	1,809	5.25	36,239	1,944	5.36
North America	HSBC Bank USA	**149,217**	**5,899**	**3.95**	131,340	6,675	5.08	130,863	7,506	5.74
	HSBC Finance	**83,834**	**7,864**	**9.38**	106,553	10,067	9.45	146,503	16,041	10.95
	HSBC Bank Canada	**65,780**	**1,936**	**2.94**	57,061	1,723	3.02	59,747	2,784	4.66
Latin America	HSBC Mexico	**22,882**	**2,097**	**9.16**	19,961	2,084	10.44	24,597	3,058	12.43
	Brazilian operations[65]	**50,202**	**7,812**	**15.56**	37,198	6,363	17.11	35,797	6,830	19.08
	HSBC Bank Panama	**12,537**	**873**	**6.96**	12,465	922	7.40	12,178	910	7.47
	HSBC Bank Argentina	**3,086**	**445**	**14.42**	2,428	421	17.34	3,093	469	15.16
Other operations		**1,417**	**2,855**		(15,184)	2,727		(45,381)	133	
		1,472,294	**58,345**	**3.96**	1,384,705	62,096	4.48	1,466,622	91,301	6.23

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Equity and liabilities

		2010			2009			2008		
		Average balance US$m	**Interest expense US$m**	**Cost %**	Average balance US$m	Interest expense US$m	Cost %	Average balance US$m	Interest expense US$m	Cost %
Summary										
Total interest-bearing liabilities (itemised below)		**1,339,390**	**18,904**	**1.41**	1,353,283	21,366	1.58	1,451,842	48,738	3.36
Trading liabilities		**258,348**	**3,497**	**1.35**	205,670	3,987	1.94	277,940	11,029	3.97
Financial liabilities designated at fair value (excluding own debt issued)		**17,456**	**283**	**1.62**	15,688	293	1.87	21,266	345	1.62
Non-interest bearing current accounts		**142,579**			123,271			98,193		
Total equity and other non-interest bearing liabilities		**741,127**			748,074			659,747		
Total equity and liabilities		**2,498,900**	**22,684**	**0.91**	2,445,986	25,646	1.05	2,508,988	60,112	2.40
Deposits by banks[66]										
Europe	HSBC Bank	**32,850**	**260**	**0.79**	35,207	553	1.57	48,167	1,875	3.89
	HSBC Private Banking Holdings (Suisse)	**964**	**2**	**0.21**	1,063	1	0.09	4,493	105	2.34
	HSBC France	**42,399**	**340**	**0.80**	43,682	536	1.23	37,851	1,672	4.42
Hong Kong	Hang Seng Bank	**1,456**	**4**	**0.27**	1,051	5	0.48	1,696	55	3.24
	The Hongkong and Shanghai	**5,691**	**10**	**0.18**	6,892	9	0.13	3,665	70	1.91

	Banking Corporation									
Rest of Asia-Pacific	The Hongkong and Shanghai Banking Corporation	**9,540**	**131**	**1.37**	10,710	165	1.54	16,232	450	2.77
	HSBC Bank Malaysia	**164**	**4**	**2.44**	110	2	1.82	338	10	2.96
Middle East	HSBC Bank Middle East	**762**	**6**	**0.79**	773	9	1.16	1,680	29	1.73
North America	HSBC Bank USA	**8,693**	**26**	**0.30**	8,381	9	0.11	11,015	220	2.00
	HSBC Bank Canada	**946**	**5**	**0.53**	1,405	8	0.57	1,391	41	2.95
Latin America	HSBC Mexico	**1,002**	**51**	**5.09**	1,462	49	3.35	822	32	3.89
	Brazilian operations[65]	**3,610**	**247**	**6.84**	3,292	241	7.32	2,790	190	6.81
	HSBC Bank Panama	**612**	**18**	**2.94**	908	26	2.86	1,016	43	4.23
	HSBC Bank Argentina	**17**	**1**	**5.88**	12	1	8.33	27	1	3.70
Other operations		**2,737**	**31**	**1.13**	2,899	45	1.55	4,564	166	3.64
		111,443	**1,136**	**1.02**	117,847	1,659	1.41	135,747	4,959	3.65
Financial liabilities designated at fair value own debt issued[67]										
Europe	HSBC Holdings	**16,577**	**308**	**1.86**	17,887	369	2.06	18,675	721	3.86
	HSBC Bank	**15,169**	**270**	**1.78**	7,932	196	2.47	8,805	529	6.01
	HSBC France	**7,154**	**113**	**1.58**	5,108	128	2.51	1,515	79	5.21
Hong Kong	Hang Seng Bank	**63**			130	2	1.54	127	6	4.72
North America	HSBC Bank USA	**1,721**	**25**	**1.45**	1,615	30	1.86	1,504	67	4.45
		24,740	**528**	**2.13**	26,628	871	3.27	32,126	1,563	4.87

HSBC
Finance

Other operations	**1,282**	**27**	**2.11**	921	(38)	(4.13)	1,083	168	15.51
	66,706	**1,271**	**1.91**	60,221	1,558	2.59	63,835	3,133	4.91

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Report of the Directors: Operating and Financial Review (continued)

Equity and liabilities (continued)

		2010			2009			2008		
		Average balance US$m	**Interest expense US$m**	**Cost %**	Average Balance US$m	Interest expense US$m	Cost %	Average balance US$m	Interest expense US$m	Cost %
Customer accounts[68]										
Europe	HSBC Bank	**275,153**	**2,042**	**0.74**	274,949	2,407	0.88	305,702	10,092	3.30
	HSBC Private Banking Holdings (Suisse)	**20,530**	**144**	**0.70**	27,250	256	0.94	37,778	1,349	3.57
	HSBC France	**50,096**	**377**	**0.75**	61,465	645	1.05	39,428	1,583	4.01
Hong Kong	Hang Seng Bank	**76,708**	**205**	**0.27**	71,140	200	0.28	66,142	914	1.38
	The Hongkong and Shanghai Banking Corporation	**160,794**	**146**	**0.09**	150,520	211	0.14	139,169	1,365	0.98
Rest of Asia-Pacific	The Hongkong and Shanghai Banking Corporation	**104,648**	**1,696**	**1.62**	92,305	1,494	1.62	96,476	2,869	2.97
	HSBC Bank Malaysia	**11,213**	**220**	**1.96**	9,658	191	1.98	10,266	295	2.87
Middle East	HSBC Bank Middle East	**15,906**	**284**	**1.79**	18,726	432	2.31	19,922	422	2.12
North America	HSBC Bank USA	**85,946**	**540**	**0.63**	85,007	975	1.15	86,701	2,069	2.39
	HSBC Bank Canada	**41,153**	**304**	**0.74**	35,051	385	1.10	34,090	967	2.84
Latin America	HSBC Mexico	**14,127**	**398**	**2.82**	11,636	391	3.36	14,612	561	3.84
	Brazilian operations[65]	**36,727**	**3,502**	**9.54**	28,605	2,946	10.30	26,288	3,110	11.83
		8,771	**321**	**3.66**	8,592	353	4.11	7,761	296	3.81

	HSBC Bank Panama									
	HSBC Bank Argentina	**2,538**	**97**	**3.82**	2,151	99	4.60	2,266	145	6.40
Other operations		**58,303**	**502**	**0.86**	63,863	361	0.57	64,253	1,952	3.04
		962,613	**10,778**	**1.12**	940,918	11,346	1.21	950,854	27,989	2.94
Debt securities in issue										
Europe	HSBC Bank	**62,735**	**1,130**	**1.80**	72,955	1,305	1.79	86,216	4,001	4.64
	HSBC France	**20,686**	**160**	**0.77**	25,065	330	1.32	30,815	1,447	4.70
	HSBC Finance							215	8	3.72
Hong Kong	Hang Seng Bank	**1,034**	**13**	**1.26**	1,220	21	1.72	1,685	57	3.38
Rest of Asia-Pacific	The Hongkong and Shanghai Banking Corporation	**5,558**	**218**	**3.92**	5,409	218	4.03	8,995	640	7.12
	HSBC Bank Malaysia	**389**	**15**	**3.86**	403	16	3.97	475	20	4.21
Middle East	HSBC Bank Middle East	**3,940**	**63**	**1.60**	2,988	62	2.07	2,650	90	3.40
North America	HSBC Bank USA	**12,680**	**375**	**2.96**	20,968	590	2.81	21,922	852	3.89
	HSBC Finance	**48,561**	**1,766**	**3.64**	63,563	2,510	3.95	98,096	3,765	3.84
	HSBC Bank Canada	**13,205**	**343**	**2.60**	12,825	322	2.51	16,957	604	3.56
Latin America	HSBC Mexico	**922**	**51**	**5.53**	1,460	67	4.59	2,693	243	9.02
	Brazilian operations[65]	**2,112**	**151**	**7.15**	1,568	86	5.48	1,859	156	8.39
	HSBC Bank Panama	**771**	**40**	**5.19**	487	34	6.98	556	33	5.94
	HSBC Bank Argentina	**4**			1			2		
Other operations		**17,301**	**606**	**3.50**	16,745	340	2.03	13,691	66	0.48
		189,898	**4,931**	**2.60**	225,657	5,901	2.62	286,827	11,982	4.18

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		2010			2009			2008		
		Average balance US$m	**Interest expense US$m**	**Cost %**	Average balance US$m	Interest expense US$m	Cost %	Average balance US$m	Interest expense US$m	Cost %
Other interest-bearing liabilities										
Europe	HSBC Bank	**28,269**	**434**	**1.54**	50,247	655	1.30	38,906	1,134	2.91
	HSBC Private Banking Holdings (Suisse)	**2,921**	**7**	**0.24**	3,892	18	0.46	4,203	135	3.21
	HSBC France	**16,668**	**78**	**0.47**	24,699	187	0.76	33,920	1,361	4.01
	HSBC Finance	**1,595**	**15**	**0.94**	2,363	59	2.50	3,712	191	5.15
Hong Kong	Hang Seng Bank	**829**	**5**	**0.60**	789	5	0.63	1,258	41	3.26
	The Hongkong and Shanghai Banking Corporation	**8,580**	**55**	**0.64**	12,815	105	0.82	10,557	288	2.73
Rest of Asia-Pacific	The Hongkong and Shanghai Banking Corporation	**34,027**	**248**	**0.73**	19,447	177	0.91	23,685	466	1.97
	HSBC Bank Malaysia	**706**	**8**	**1.13**	266	2	0.75	338	7	2.07
Middle East	HSBC Bank Middle East	**1,496**	**63**	**4.21**	1,748	68	3.89	1,918	89	4.64
North America	HSBC Bank USA	**14,669**	**609**	**4.15**	9,754	368	3.77	10,490	468	4.46

	HSBC Finance	**3,487**	**102**	**2.93**	4,051	102	2.52	4,670	141	3.02
	HSBC Bank Canada	**1,806**	**3**	**0.17**	1,149	6	0.52	1,306	19	1.45
	HSBC Markets Inc	**1,266**	**25**	**1.97**	1,716	36	2.10	10,349	78	0.75
Latin America	HSBC Mexico	**804**	**13**	**1.62**	301	11	3.65	187	20	10.70
	Brazilian operations[65]	**2,803**	**316**	**11.27**	1,496	130	8.69	2,340	207	8.85
	HSBC Bank Panama	**108**	**1**	**0.93**	192	2	1.04	917	3	0.33
	HSBC Bank Argentina	**4**			36	1	2.78	92	6	6.52
Other operations		**(111,308)**	**(1,194)**		(126,321)	(1,030)		(134,269)	(3,979)	
		8,730	**788**	**9.03**	8,640	902	10.44	14,579	675	4.63
Total interest-bearing liabilities										
Europe	HSBC Bank	**414,176**	**4,136**	**1.00**	441,290	5,116	1.16	487,796	17,631	3.61
	HSBC Private Banking Holdings (Suisse)	**24,415**	**153**	**0.63**	32,205	275	0.85	46,474	1,589	3.42
	HSBC France	**137,003**	**1,068**	**0.78**	160,019	1,826	1.14	143,529	6,142	4.28
	HSBC Finance	**1,595**	**15**	**0.94**	2,363	59	2.50	3,927	199	5.07
Hong Kong	Hang Seng Bank	**80,090**	**227**	**0.28**	74,330	233	0.31	70,908	1,073	1.51
	The Hongkong and Shanghai Banking Corporation	**175,065**	**211**	**0.12**	170,227	325	0.19	153,391	1,723	1.12
Rest of Asia-Pacific	The Hongkong and Shanghai Banking Corporation	**153,773**	**2,293**	**1.49**	127,871	2,054	1.61	145,388	4,425	3.04

	HSBC Bank Malaysia	**12,472**	**247**	**1.98**	10,437	211	2.02	11,417	332	2.91
Middle East	HSBC Bank Middle East	**22,104**	**416**	**1.88**	24,235	571	2.36	26,170	630	2.41
North America	HSBC Bank USA	**123,709**	**1,575**	**1.27**	125,725	1,972	1.57	131,632	3,676	2.79
	HSBC Finance	**76,788**	**2,396**	**3.12**	94,242	3,483	3.70	134,892	5,469	4.05
	HSBC Bank Canada	**57,110**	**655**	**1.15**	50,430	721	1.43	53,744	1,631	3.03
	HSBC Markets Inc	**1,266**	**25**	**1.97**	1,716	36	2.10	10,349	78	0.75
Latin America	HSBC Mexico	**16,855**	**513**	**3.04**	14,859	518	3.49	18,314	856	4.67
	Brazilian operations[65]	**45,252**	**4,216**	**9.32**	34,961	3,403	9.73	33,277	3,663	11.01
	HSBC Bank Panama	**10,262**	**379**	**3.69**	10,179	415	4.08	10,250	375	3.66
	HSBC Bank Argentina	**2,563**	**98**	**3.82**	2,200	101	4.59	2,387	152	6.37
Other operations		**(15,108)**	**281**		(24,006)	47		(32,003)	(906)	
		1,339,390	**18,904**	**1.41**	1,353,283	21,366	1.58	1,451,842	48,738	3.36

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Net interest margin[69]

		2010 %	2009 %	2008 %
Total		**2.68**	2.94	2.90
Europe	HSBC Bank	**2.12**	2.35	1.71
	HSBC Private Banking Holdings (Suisse)	**1.18**	1.30	1.24
	HSBC France	**0.90**	0.68	0.26
	HSBC Finance	**8.13**	8.40	6.36
Hong Kong	Hang Seng Bank	**1.91**	2.11	2.59
	The Hongkong and Shanghai Banking Corporation	**1.38**	1.52	2.27
Rest of Asia-Pacific	The Hongkong and Shanghai Banking Corporation	**1.98**	2.15	2.15
	HSBC Bank Malaysia	**2.76**	2.72	3.02
Middle East	HSBC Bank Middle East	**3.12**	3.59	3.63
North America	HSBC Bank USA	**2.90**	3.58	2.93
	HSBC Finance	**6.52**	6.18	7.22
	HSBC Bank Canada	**1.95**	1.76	1.93
Latin America	HSBC Mexico	**6.92**	7.85	8.95
	Brazilian operations[65]	**7.16**	7.96	8.85
	HSBC Bank Panama	**3.94**	4.07	4.39
	HSBC Bank Argentina	**11.24**	13.18	10.25

Distribution of average total assets

		2010 %	2009 %	2008 %
Europe	HSBC Bank	**37.5**	36.7	36.7
	HSBC Private Banking Holdings (Suisse)	**2.2**	2.3	2.3
	HSBC France	**12.9**	15.0	13.8
	HSBC Finance	**0.1**		0.2
Hong Kong	Hang Seng Bank	**4.5**	4.2	3.9
	The Hongkong and Shanghai Banking Corporation	**10.7**	10.5	9.5

Rest of Asia-Pacific	The Hongkong and Shanghai Banking Corporation	**9.4**	8.5	8.8
	HSBC Bank Malaysia	**0.7**	0.6	0.6
Middle East	HSBC Bank Middle East	**1.6**	1.6	1.8
North America	HSBC Bank USA	**9.7**	11.0	11.2
	HSBC Finance	**3.6**	4.5	6.2
	HSBC Bank Canada	**3.0**	2.7	2.9
Latin America	HSBC Mexico	**1.4**	1.4	1.5
	Brazilian operations[65]	**2.6**	2.1	2.1
	HSBC Bank Panama	**0.6**	0.6	0.6
	HSBC Bank Argentina	**0.2**	0.2	0.2
Other operations (including consolidation adjustments)		**(0.7)**	(1.9)	(2.3)
		100.0	100.0	100.0

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Analysis of changes in net interest income and net interest expense
The following tables allocate changes in net interest income and net interest expense between volume and rate for 2010 compared with 2009, and for 2009 compared with 2008.
Interest income

			Increase/(decrease) in 2010 compared with 2009			Increase/(decrease) in 2009 compared with 2008		
		2010	**Volume**	**Rate**	2009	Volume	Rate	2008
		US$m	**US$m**	**US$m**	US$m	US$m	US$m	US$m
Short term funds and loans and advances to banks								
Europe	HSBC Bank	**1,290**	**333**	**(422)**	1,379	(386)	(422)	2,187
	HSBC Private Banking Holdings (Suisse)	**15**	**(18)**	**(10)**	43	(149)	(141)	333
	HSBC France	**337**	**116**	**(219)**	440	60	(1,115)	1,495
Hong Kong	Hang Seng Bank	**222**	**(21)**	**41**	202	(26)	(359)	587
	The Hongkong and Shanghai Banking Corporation	**117**	**(74)**	**9**	182	(549)	(613)	1,344
Rest of Asia-Pacific	The Hongkong and Shanghai Banking Corporation	**464**	**101**	**37**	326	(152)	(403)	881
	HSBC Bank Malaysia	**126**	**29**	**16**	81	(31)	(53)	165
Middle East	HSBC Bank Middle East	**60**	**12**	**(4)**	52	(54)	(82)	188
North America	HSBC Bank USA	**103**	**1,058**	**(1,049)**	94	(248)	14	328
	HSBC Bank Canada	**16**	**3**	**3**	10	(13)	(84)	107
Latin America	HSBC Mexico	**129**	**(19)**	**(1)**	149	3	(101)	247
	Brazilian operations[65]	**1,525**	**537**	**(15)**	1,003	302	(250)	951
	HSBC Bank Panama	**8**	**(2)**		10	1	(21)	30
	HSBC Bank Argentina	**20**	**(10)**	**1**	29	(25)	11	43
Other operations		**123**	**(20)**	**(56)**	199	(160)	(401)	760

		4,555	**963**	**(607)**	4,199	(1,911)	(3,536)	9,646
Loans and advances to customers								
Europe	HSBC Bank	**9,761**	**(451)**	**(686)**	10,898	(749)	(6,940)	18,587
	HSBC Private Banking Holdings (Suisse)	**191**	**35**	**(20)**	176	(94)	(224)	494
	HSBC France	**1,684**	**(113)**	**(135)**	1,932	(118)	(1,554)	3,604
	HSBC Finance	**198**	**(87)**	**(34)**	319	(180)	(6)	505
Hong Kong	Hang Seng Bank	**1,313**	**235**	**(116)**	1,194	12	(407)	1,589
	The Hongkong and Shanghai Banking Corporation	**1,755**	**316**	**(318)**	1,757	28	(562)	2,291
Rest of Asia-Pacific	The Hongkong and Shanghai Banking Corporation	**3,928**	**821**	**(561)**	3,668	(762)	(733)	5,163
	HSBC Bank Malaysia	**531**	**84**	**(8)**	455	(19)	(79)	553
Middle East	HSBC Bank Middle East	**1,303**	**(100)**	**(190)**	1,593	(71)	115	1,549
North America	HSBC Bank USA	**4,582**	**(1,118)**	**159**	5,541	330	(547)	5,758
	HSBC Finance	**7,741**	**(2,264)**	**64**	9,941	(4,472)	(1,422)	15,835
	HSBC Bank Canada	**1,643**	**114**	**30**	1,499	(267)	(689)	2,455
Latin America	HSBC Mexico	**1,571**	**17**	**(154)**	1,708	(753)	(104)	2,565
	Brazilian operations[65]	**5,118**	**1,120**	**(496)**	4,494	(233)	(152)	4,879
	HSBC Bank Panama	**815**	**4**	**(53)**	864	64	(10)	810
	HSBC Bank Argentina	**367**	**96**	**(86)**	357	(35)	14	378
Other operations		**1,685**	**249**	**(469)**	1,905	100	98	1,707
		44,186	**(641)**	**(3,474)**	48,301	(5,358)	(15,063)	68,722

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Interest income (continued)

			Increase/(decrease) in 2010 compared with 2009			Increase/(decrease) in 2009 compared with 2008		
		2010	**Volume**	**Rate**	2009	Volume	Rate	2008
		US$m	**US$m**	**US$m**	US$m	US$m	US$m	US$m
Financial investments								
Europe	HSBC Bank	**1,725**	**158**	**(754)**	2,321	(182)	(1,337)	3,840
	HSBC Private Banking Holdings (Suisse)	**287**	**33**	**(109)**	363	165	(355)	553
	HSBC France	**102**	**(35)**	**(4)**	141	(510)	(144)	795
Hong Kong	Hang Seng Bank	**541**	**147**	**(236)**	630	25	(458)	1,063
	The Hongkong and Shanghai Banking Corporation	**477**	**150**	**(317)**	644	1,380	(1,299)	563
Rest of Asia-Pacific	The Hongkong and Shanghai Banking Corporation	**1,161**	**115**	**7**	1,039	97	(565)	1,507
	HSBC Bank Malaysia	**28**	**(9)**		37	11	(10)	36
Middle East	HSBC Bank Middle East	**126**	**18**	**(10)**	118	34	(60)	144
North America	HSBC Bank USA	**1,156**	**402**	**(215)**	969	106	(369)	1,232
	HSBC Finance	**116**	**20**	**(24)**	120	(24)	1	143
	HSBC Bank Canada	**257**	**80**	**(28)**	205	91	(83)	197
Latin America	HSBC Mexico	**388**	**189**	**(28)**	227	31	(48)	244
	Brazilian operations[65]	**1,089**	**312**	**(43)**	820	22	(55)	853
	HSBC Bank Panama	**38**	**25**	**(26)**	39	(1)	(7)	47
	HSBC Bank Argentina	**58**	**37**	**(14)**	35	(17)	5	47
Other operations		**1,826**	**195**	**(86)**	1,717	966	(603)	1,354
		9,375	**1,638**	**(1,688)**	9,425	2,790	(5,983)	12,618

For footnotes, see page 83.

Interest expense

			Increase/(decrease) in 2010 compared with 2009			Increase/(decrease) in 2009 compared with 2008		
		2010 US$m	**Volume US$m**	**Rate US$m**	2009 US$m	Volume US$m	Rate US$m	2008 US$m
Deposits by banks								
Europe	HSBC Bank	**260**	**(37)**	**(256)**	553	(504)	(818)	1,875
	HSBC Private Banking Holdings (Suisse)	**2**		**1**	1	(80)	(24)	105
	HSBC France	**340**	**(16)**	**(180)**	536	258	(1,394)	1,672
Hong Kong	Hang Seng Bank	**4**	**2**	**(3)**	5	(21)	(29)	55
	The Hongkong and Shanghai Banking Corporation	**10**	**(2)**	**3**	9	62	(123)	70
Rest of Asia-Pacific	The Hongkong and Shanghai Banking Corporation	**131**	**(18)**	**(16)**	165	(153)	(132)	450
	HSBC Bank Malaysia	**4**	**1**	**1**	2	(7)	(1)	10
Middle East	HSBC Bank Middle East	**6**		**(3)**	9	(16)	(4)	29
North America	HSBC Bank USA	**26**		**17**	9	(53)	(158)	220
	HSBC Bank Canada	**5**	**(3)**		8		(33)	41
Latin America	HSBC Mexico	**51**	**(15)**	**17**	49	25	(8)	32
	Brazilian operations[65]	**247**	**23**	**(17)**	241	34	17	190
	HSBC Bank Panama	**18**	**(8)**		26	(5)	(12)	43
	HSBC Bank Argentina	**1**			1	(1)	1	1
Other operations		**31**	**(3)**	**(11)**	45	(61)	(60)	166
		1,136	**(90)**	**(433)**	1,659	(653)	(2,647)	4,959

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			Increase/(decrease) in 2010 compared with 2009			Increase/(decrease) in 2009 compared with 2008		
		2010	**Volume**	**Rate**	2009	Volume	Rate	2008
		US$m	**US$m**	**US$m**	US$m	US$m	US$m	US$m
Customer accounts								
Europe	HSBC Bank	**2,042**	**2**	**(367)**	2,407	(1,015)	(6,670)	10,092
	HSBC Private Banking Holdings (Suisse)	**144**	**(63)**	**(49)**	256	(376)	(717)	1,349
	HSBC France	**377**	**(119)**	**(149)**	645	884	(1,822)	1,583
Hong Kong	Hang Seng Bank	**205**	**16**	**(11)**	200	69	(783)	914
	The Hongkong and Shanghai Banking Corporation	**146**	**14**	**(79)**	211	111	(1,265)	1,365
Rest of Asia-Pacific	The Hongkong and Shanghai Banking Corporation	**1,696**	**200**	**2**	1,494	(124)	(1,251)	2,869
	HSBC Bank Malaysia	**220**	**31**	**(2)**	191	(17)	(87)	295
Middle East	HSBC Bank Middle East	**284**	**(65)**	**(83)**	432	(25)	35	422
North America	HSBC Bank USA	**540**	**11**	**(446)**	975	(40)	(1,054)	2,069
	HSBC Bank Canada	**304**	**67**	**(148)**	385	27	(609)	967
Latin America	HSBC Mexico	**398**	**84**	**(77)**	391	(114)	(56)	561
	Brazilian operations[65]	**3,502**	**837**	**(281)**	2,946	274	(438)	3,110
	HSBC Bank Panama	**321**	**7**	**(39)**	353	32	25	296
	HSBC Bank Argentina	**97**	**18**	**(20)**	99	(7)	(39)	145
Other operations		**502**	**(32)**	**173**	361	(12)	(1,579)	1,952
		10,778	**263**	**(831)**	11,346	(292)	(16,351)	27,989
Financial liabilities designated at fair value own debt issued		**1,271**	**168**	**(455)**	1,558	(177)	(1,398)	3,133

Debt securities in issue

Europe	HSBC Bank	**1,130**	**(183)**	**8**	1,305	(615)	(2,081)	4,001
	HSBC France	**160**	**(58)**	**(112)**	330	(270)	(847)	1,447
	HSBC Finance					(8)		8
Hong Kong	Hang Seng Bank	**13**	**(3)**	**(5)**	21	(16)	(20)	57
Rest of Asia-Pacific	The Hongkong and Shanghai Banking Corporation	**218**	**6**	**(6)**	218	(255)	(167)	640
	HSBC Bank Malaysia	**15**	**(1)**		16	(3)	(1)	20
Middle East	HSBC Bank Middle East	**63**	**20**	**(19)**	62	11	(39)	90
North America	HSBC Bank USA	**375**	**(233)**	**18**	590	(37)	(225)	852
	HSBC Finance	**1,766**	**(593)**	**(151)**	2,510	(1,326)	71	3,765
	HSBC Bank Canada	**343**	**10**	**11**	322	(147)	(135)	604
Latin America	HSBC Mexico	**51**	**(25)**	**9**	67	(111)	(65)	243
	Brazilian operations[65]	**151**	**30**	**35**	86	(24)	(46)	156
	HSBC Bank Panama	**40**	**20**	**(14)**	34	(4)	5	33
Other operations		**606**	**11**	**255**	340	15	259	66
		4,931	**(937)**	**(33)**	5,901	(2,557)	(3,524)	11,982

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Short-term borrowings
We include short-term borrowings within customer accounts, deposits by banks and debt securities in issue and do not show short-term borrowings separately on the balance sheet. Short-term borrowings are defined by the US Securities and
Exchange Commission as Federal funds purchased and securities sold under agreements to repurchase, commercial paper and other short-term borrowings. Our only significant short-term borrowings are securities sold under agreements to repurchase and certain debt securities in issue. Additional information on these is provided in the table below.

Repos and short-term bonds

	2010	2009	2008
	US$	US$m	US$m
Securities sold under agreements to repurchase			
Outstanding at 31 December	**159,256**	152,218	145,180
Average amount outstanding during the year	**175,955**	170,671	177,256
Maximum quarter-end balance outstanding during the year	**193,319**	157,778	190,651
Weighted average interest rate during the year	**0.5%**	0.8%	3.8%
Weighted average interest rate at the year-end	**0.9%**	0.4%	2.9%
Short-term bonds			
Outstanding at 31 December	**44,152**	38,776	40,279
Average amount outstanding during the year	**37,981**	33,010	45,330
Maximum quarter-end balance outstanding during the year	**44,152**	38,776	55,842
Weighted average interest rate during the year	**2.9%**	3.2%	5.0%
Weighted average interest rate at the year-end	**4.5%**	0.6%	3.1%

Contractual obligations
The table below provides details of our material contractual obligations as at 31 December 2010.

		Payments due by period		
	Total	**Less than 1 year**	**1 5 years**	**More than 5 years**
	US$m	**US$m**	**US$m**	**US$m**
Long-term debt obligations	**236,144**	**71,913**	**90,284**	**73,947**
Term deposits and certificates of deposit	**207,805**	**193,131**	**10,643**	**4,031**
Capital (finance) lease obligations	**684**	**107**	**187**	**390**
Operating lease obligations	**6,257**	**943**	**2,700**	**2,614**
Purchase obligations	**1,071**	**657**	**414**	

Short positions in debt securities and equity shares	**102,615**	**74,979**	**8,412**	**19,224**
Current tax liability	**1,804**	**1,804**		
Pension/healthcare obligation	**16,643**	**1,304**	**5,700**	**9,639**
	573,023	**344,838**	**118,340**	**109,845**

Ratios of earnings to combined fixed charges (and preference share dividends)

	2010	2009	2008	2007	2006
Ratios of earnings to combined fixed charges and preference share dividends:[70]					
excluding interest on deposits	**5.89**	2.64	2.97	6.96	7.22
including interest on deposits	**1.69**	1.20	1.13	1.34	1.40
Ratios of earnings to combined fixed charges:[70]					
excluding interest on deposits	**7.10**	2.99	3.17	7.52	7.93
including interest on deposits	**1.73**	1.22	1.14	1.34	1.41

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Loan maturity and interest sensitivity analysis
At 31 December 2010, the geographical analysis of loan maturity and interest sensitivity by loan type on a contractual repayment basis was as follows:

	Europe US$m	Hong Kong US$m	Rest of Asia-Pacific US$m	Middle East US$m	North America US$m	Latin America US$m	Total US$m
Maturity of 1 year or less							
Loans and advances to banks	**75,280**	**32,974**	**40,116**	**9,034**	**18,820**	**24,032**	**200,256**
Commercial loans to customers							
Commercial, industrial and international trade	**72,108**	**25,889**	**34,536**	**8,139**	**7,242**	**14,215**	**162,129**
Real estate and other property related	**16,040**	**10,739**	**5,753**	**1,635**	**5,892**	**1,851**	**41,910**
Non-bank financial institutions	**64,313**	**1,994**	**1,641**	**785**	**13,126**	**1,137**	**82,996**
Governments	**1,432**	**38**	**178**	**1,170**	**41**	**513**	**3,372**
Other commercial	**31,377**	**4,383**	**6,759**	**1,830**	**5,641**	**3,440**	**53,430**
	185,270	**43,043**	**48,867**	**13,559**	**31,942**	**21,156**	**343,837**
Hong Kong Government Home Ownership Scheme		**370**					**370**
Residential mortgages and other personal loans	**29,904**	**15,337**	**12,161**	**2,819**	**31,174**	**9,190**	**100,585**
Loans and advances to customers	**215,174**	**58,750**	**61,028**	**16,378**	**63,116**	**30,346**	**444,792**
	290,454	**91,724**	**101,144**	**25,412**	**81,936**	**54,378**	**645,048**
Maturity after 1 year but within 5 years							
Loans and advances to banks	**2,499**	**204**	**285**	**234**	**626**	**487**	**4,335**
Commercial loans to customers							
Commercial, industrial and international trade	**29,641**	**6,920**	**6,178**	**2,371**	**7,859**	**6,086**	**59,055**
Real estate and other property related	**13,901**	**16,940**	**7,630**	**1,202**	**6,057**	**1,524**	**47,254**
Non-bank financial institutions	**4,866**	**748**	**362**	**540**	**6,689**	**1,161**	**14,366**
Governments	**309**	**2,188**	**159**	**165**	**40**	**843**	**3,704**

Other commercial	**13,573**	**4,509**	**4,306**	**1,692**	**2,113**	**2,821**	**29,014**
	62,290	**31,305**	**18,635**	**5,970**	**22,758**	**12,435**	**153,393**
Hong Kong Government Home Ownership Scheme		**1,228**					**1,228**
Residential mortgages and other personal loans	**33,732**	**10,922**	**8,301**	**1,741**	**38,223**	**6,572**	**99,491**
Loans and advances to customers	**96,022**	**43,455**	**26,936**	**7,711**	**60,981**	**19,007**	**254,112**
	98,521	**43,659**	**27,221**	**7,945**	**61,607**	**19,494**	**258,447**
Interest rate sensitivity of loans and advances to banks and commercial loans to customers							
Fixed interest rate	**17,263**	**78**	**1,233**	**1,358**	**8,209**	**3,432**	**31,573**
Variable interest rate	**47,526**	**31,431**	**17,687**	**4,846**	**15,175**	**9,490**	**126,155**
	64,789	**31,509**	**18,920**	**6,204**	**23,384**	**12,922**	**157,728**
Maturity after 5 years							
Loans and advances to banks	**460**	**407**	**36**	**67**	**33**	**2,835**	**3,838**
Commercial loans to customers							
Commercial, industrial and international trade	**10,231**	**642**	**560**	**663**	**1,636**	**2,778**	**16,510**
Real estate and other property related	**7,089**	**7,231**	**775**	**33**	**1,928**	**498**	**17,554**
Non-bank financial institutions	**840**	**82**	**55**	**10**	**1,294**	**520**	**2,801**
Governments	**548**	**113**	**78**	**10**	**8**	**761**	**1,518**
Other commercial	**13,477**	**1,596**	**536**	**662**	**1,019**	**226**	**17,516**
	32,185	**9,664**	**2,004**	**1,378**	**5,885**	**4,783**	**55,899**
Hong Kong Government Home Ownership Scheme		**1,939**					**1,939**
Residential mortgages and other personal loans	**98,081**	**27,512**	**19,722**	**811**	**69,720**	**5,861**	**221,707**
Loans and advances to customers	**130,266**	**39,115**	**21,726**	**2,189**	**75,605**	**10,644**	**279,545**
	130,726	**39,522**	**21,762**	**2,256**	**75,638**	**13,479**	**283,383**

Interest rate sensitivity of loans and advances to banks and commercial loans to customers							
Fixed interest rate	**8,326**	**412**	**108**	**855**	**1,669**	**2,369**	**13,739**
Variable interest rate	**24,319**	**9,659**	**1,932**	**590**	**4,249**	**5,249**	**45,998**
	32,645	**10,071**	**2,040**	**1,445**	**5,918**	**7,618**	**59,737**

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Deposits

The following tables summarise the average amount of bank deposits, customer deposits and certificates of deposit (CD s) and other money market instruments (which are included within Debt securities in issue in the balance sheet), together
with the average interest rates paid thereon for each of the past three years. The geographical analysis of average deposits is based on the location of the office in which the deposits are recorded and excludes balances with HSBC companies. The Other category includes securities sold under agreements to repurchase.

Deposits by banks

	2010		2009		2008	
	Average balance US$m	**Average rate %**	Average balance US$m	Average rate %	Average balance US$m	Average rate %
Europe	**85,973**		87,677		99,228	
Demand and other non-interest bearing	**8,298**		6,415		5,231	
Demand interest bearing	**13,783**	**0.6**	14,259	1.0	19,204	3.2
Time	**28,337**	**0.9**	30,367	1.6	43,695	3.9
Other	**35,555**	**0.8**	36,636	1.3	31,098	4.4
Hong Kong	**10,000**		10,725		5,916	
Demand and other non-interest bearing	**2,860**		2,975		1,375	
Demand interest bearing	**4,787**	**0.2**	5,526	0.1	2,780	2.0
Time	**1,803**	**0.3**	1,637	0.3	1,583	2.7
Other	**550**	**0.7**	587	0.5	178	3.4
Rest of Asia-Pacific	**11,476**		12,467		18,203	
Demand and other non-interest bearing	**1,746**		1,605		1,546	
Demand interest bearing	**4,937**	**1.2**	4,097	1.2	4,317	2.3
Time	**3,626**	**1.5**	4,682	1.9	9,103	3.5
Other	**1,167**	**2.0**	2,083	1.4	3,237	3.8
Middle East	**1,250**		1,317		2,151	
Demand and other non-interest bearing	**484**		539		365	

Demand interest bearing	**9**		18		15	
Time	**685**	**0.6**	691	1.2	1,239	2.7
Other	**72**	**1.2**	69	1.4	532	0.2
North America	**13,324**		13,203		14,835	
Demand and other non-interest bearing	**2,493**		1,755		761	
Demand interest bearing	**3,386**	**0.1**	4,770	0.1	5,684	1.7
Time	**4,716**	**0.4**	5,422	0.2	7,941	2.3
Other	**2,729**	**0.5**	1,256	0.7	449	1.6
Latin America	**5,523**		5,959		5,058	
Demand and other non-interest bearing	**222**		212		366	
Demand interest bearing	**322**	**4.3**	219	0.9	81	2.5
Time	**2,246**	**5.5**	4,171	5.0	3,357	5.6
Other	**2,733**	**6.6**	1,357	8.1	1,254	7.8
Total	**127,546**		131,348		145,391	
Demand and other non-interest bearing	**16,103**		13,501		9,644	
Demand interest bearing	**27,224**	**0.6**	28,889	0.7	32,081	2.7
Time	**41,413**	**1.1**	46,970	1.7	66,918	3.7
Other	**42,806**	**1.3**	41,988	1.6	36,748	4.5

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Customer accounts

	2010		2009		2008	
	Average balance US$m	**Average rate %**	Average balance US$m	Average rate %	Average balance US$m	Average rate %
Europe	**424,561**		440,450		447,982	
Demand and other non-interest bearing	**62,869**		55,751		39,610	
Demand interest bearing	**203,727**	**0.4**	212,178	0.4	225,034	2.9
Savings	**51,793**	**1.8**	57,344	2.2	73,479	4.3
Time	**60,140**	**1.2**	67,045	1.4	83,208	3.8
Other	**46,032**	**0.5**	48,132	0.8	26,651	3.9
Hong Kong	**280,733**		261,703		236,109	
Demand and other non-interest bearing	**27,412**		22,056		15,620	
Demand interest bearing	**202,330**		171,846	0.1	126,199	0.4
Savings	**37,119**	**0.5**	45,537	0.6	65,068	2.4
Time	**12,793**	**0.7**	20,901	0.6	27,659	2.3
Other	**1,079**	**0.2**	1,363	0.1	1,563	1.2
Rest of Asia-Pacific	**142,807**		126,144		128,381	
Demand and other non-interest bearing	**16,418**		13,425		11,872	
Demand interest bearing	**63,033**	**1.0**	53,108	0.8	49,329	2.0
Savings	**51,757**	**2.4**	46,137	2.5	52,849	3.8
Time	**10,734**	**0.9**	12,542	1.2	13,342	3.3
Other	**865**	**2.2**	932	1.8	989	3.6
Middle East	**32,747**		33,211		35,546	
Demand and other non-interest bearing	**11,873**		9,865		10,849	
Demand interest bearing	**6,315**	**1.5**	6,364	1.4	6,324	1.6
Savings	**13,774**	**2.8**	15,005	3.4	16,119	3.1
Time	**604**	**2.6**	1,424	2.7	1,884	2.9
Other	**181**	**0.1**	553	0.2	370	0.5

North America	**157,361**		145,820		144,982	
Demand and other non-interest bearing	**22,235**		18,350		16,759	
Demand interest bearing	**28,569**	**0.2**	25,870	0.2	18,261	1.6
Savings	**78,040**	**0.8**	69,296	1.4	87,001	2.5
Time	**17,975**	**0.8**	25,164	1.3	17,838	3.2
Other	**10,542**	**0.6**	7,140	0.8	5,123	2.4
Latin America	**77,618**		63,635		65,071	
Demand and other non-interest bearing	**12,407**		10,598		12,507	
Demand interest bearing	**6,270**	**1.2**	4,734	1.1	4,994	1.9
Savings	**41,784**	**8.5**	33,091	8.5	31,442	10.3
Time	**15,716**	**3.9**	14,244	4.8	15,179	5.2
Other	**1,441**	**7.5**	968	6.4	949	8.2
Total	**1,115,827**		1,070,963		1,058,071	
Demand and other non-interest bearing	**153,214**		130,045		107,217	
Demand interest bearing	**510,244**	**0.3**	474,100	0.3	430,141	1.9
Savings	**274,267**	**2.5**	266,410	2.6	325,958	3.9
Time	**117,962**	**1.4**	141,320	1.6	159,110	3.6
Other	**60,140**	**0.7**	59,088	0.9	35,645	3.6

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Certificates of deposit and other money market instruments

	2010		2009		2008	
	Average balance US$m	**Average rate %**	Average balance US$m	Average rate %	Average balance US$m	Average rate %
Europe	**57,018**	**0.4**	65,151	0.9	74,007	4.5
Hong Kong	**213**	**3.8**	278	3.6	745	3.0
Rest of Asia-Pacific	**3,529**	**3.4**	3,536	3.7	6,966	6.6
Middle East	**68**	**0.5**	265	6.4	648	4.6
North America	**10,607**	**0.5**	14,218	1.1	22,278	3.3
Latin America	**1,126**	**4.0**	1,227	3.6	3,036	7.8
	72,561	**0.6**	84,675	1.2	107,680	4.5

Certificates of deposit and other time deposits

The maturity analysis of certificates of deposit (CD s) and other wholesale time deposits is expressed by remaining maturity. The majority of CDs and time deposits are in amounts of US$100,000 and over or the equivalent in other currencies.

	At 31 December 2010				
	3 months or less US$m	**After 3 months but within 6 months US$m**	**After 6 months but within 12 months US$m**	**After 12 months US$m**	**Total US$m**
Europe	**98,113**	**14,977**	**15,726**	**7,587**	**136,403**
Certificates of deposit	**14,153**	**7,660**	**6,018**		**27,831**
Time deposits:					
banks	**25,183**	**2,530**	**1,671**	**2,221**	**31,605**
customers	**58,777**	**4,787**	**8,037**	**5,366**	**76,967**
Hong Kong	**12,420**	**564**	**1,289**	**722**	**14,995**
Certificates of deposit	**87**	**45**	**6**	**314**	**452**
Time deposits:					

banks	**2,234**	**10**	**65**	**24**	**2,333**
customers	**10,099**	**509**	**1,218**	**384**	**12,210**
Rest of Asia-Pacific	**15,375**	**877**	**542**	**1,530**	**18,324**
Certificates of deposit	**3,347**	**370**	**373**	**559**	**4,649**
Time deposits:					
banks	**1,777**	**34**	**2**	**107**	**1,920**
customers	**10,251**	**473**	**167**	**864**	**11,755**
Middle East	**507**	**113**	**120**	**568**	**1,308**
Certificates of deposit					
Time deposits:					
banks	**364**		**2**	**340**	**706**
customers	**143**	**113**	**118**	**228**	**602**
North America	**12,220**	**1,979**	**1,977**	**1,152**	**17,328**
Time deposits:					
banks	**2,501**	**13**	**3**	**204**	**2,721**
customers	**9,719**	**1,966**	**1,974**	**948**	**14,607**
Latin America	**13,213**	**1,446**	**1,673**	**3,115**	**19,447**
Certificates of deposit	**183**	**53**	**447**	**382**	**1,065**
Time deposits:					
banks	**1,855**	**290**	**163**	**305**	**2,613**
customers	**11,175**	**1,103**	**1,063**	**2,428**	**15,769**
Total	**151,848**	**19,956**	**21,327**	**14,674**	**207,805**
Certificates of deposit	**17,770**	**8,128**	**6,844**	**1,255**	**33,997**
Time deposits:					
banks	**33,914**	**2,877**	**1,906**	**3,201**	**41,898**
customers	**100,164**	**8,951**	**12,577**	**10,218**	**131,910**

Economic profit

Our internal performance measures include economic profit/(loss), a calculation which compares the return on financial capital invested in HSBC by our shareholders with the cost of that capital. We price our cost of capital internally and the difference between that cost and the post-tax profit attributable to ordinary shareholders represents the amount of economic profit/(loss) generated. Economic profit/(loss) generated is used by management as one input in deciding where to allocate capital and other resources.

In order to concentrate on external factors rather than measurement bases, we emphasise the trend in economic profit/(loss) ahead of absolute amounts within business units. Our long-term cost of capital is reviewed annually and for 2010 it was revised to 11% from the 10% used in 2009. We use a Capital Asset Pricing Model to determine our cost of capital. The main drivers of the increase were an increase in the risk free rate and an increase in the betas used in the calculation. The following commentary is on a reported basis.

Our economic loss decreased by US$4.7bn to US$3.3bn as a result of an increase in profit attributable to shareholders. This was predominantly driven by lower loan impairment charges across all regions and customer groups, notably in the US due to lower balances and decreased delinquency rates in Card and Retail Services, and the run-off of the Consumer Lending and mortgage services portfolio.

The increase in average invested capital reflected higher retained earnings and a significant decrease in reserves representing unrealised losses on available-for-sale securities due to a slowing in the rate of anticipated losses in the underlying collateral pools.

The return on invested capital increased by 4.6 percentage points, although it remained below our benchmark cost of capital. The economic spread improved by 3.6 percentage points, the result of an increase in return on invested capital, partly offset by the rise in the cost of capital in 2010.

	2010		2009	
	US$m	**%**[41]	US$m	%[40]
Average total shareholders equity	**138,224**		115,431	
Adjusted by:				
Goodwill previously amortised or written off	**8,123**		8,123	
Property revaluation reserves	**(813)**		(799)	
Reserves representing unrealised losses on effective cash flow hedges	**100**		385	
Reserves representing unrealised losses on available-for-sale securities	**6,129**		16,189	
Preference shares and other equity instruments	**(5,473)**		(3,538)	
Average invested capital[42]	**146,290**		135,791	
Return on invested capital[43]	**12,746**	**8.7**	5,565	4.1

Benchmark cost of capital	**(16,092)**	**(11.0)**	(13,579)	(10.0)
Economic loss and spread	**(3,346)**	**(2.3)**	(8,014)	(5.9)

For footnotes, see page 83.

Critical accounting policies

(Audited)

Introduction

The results of HSBC are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of our consolidated financial statements. The significant accounting policies are described in Note 2 on the Financial Statements.

When preparing the financial statements, it is the Directors responsibility under UK company law to select suitable accounting policies and to make judgements and estimates that are reasonable and prudent. The accounting policies that are deemed critical to our results and financial position, in terms of the materiality of the items to which the policies are applied and the high degree of judgement involved, including the use of assumptions and estimation, are discussed below.

Impairment of loans and advances

Our accounting policy for losses arising from the impairment of customer loans and advances is described in Note 2g on the Financial Statements. Loan impairment allowances represent management s best estimate of losses incurred in the loan portfolios at the balance sheet date.

Management is required to exercise judgement in making assumptions and estimations when calculating loan impairment allowances on both individually and collectively assessed loans and advances. Of the Group s total loans and advances to customers before impairment allowances of US$978bn (2009: US$922bn), US$15bn or 2% (2009: US$15bn; 2%) were individually assessed for impairment, and US$963bn or 98% (2009: US$907bn; 98%) were collectively assessed for impairment.

The most significant judgemental area is the calculation of collective impairment allowances. The geographical area with most exposure to collectively assessed loans and advances is North America, which comprised US$198bn or 21% (2009: US$219bn; 24%) of the total. Collective impairment allowances in North America were US$9bn, representing 64% (2009: US$13bn; 68%) of the total collectively assessed loan impairment allowance.

The methods used to calculate collective impairment allowances on homogeneous groups of loans and advances that are not considered individually significant are disclosed in Note 2g on the Financial Statements. They are subject to estimation uncertainty, in part because it is not practicable to identify losses on an individual loan basis because of the large number of individually insignificant loans in the portfolio.

The methods involve the use of statistically assessed historical information which is supplemented with significant management judgement to assess whether current economic and credit conditions are such that the actual level of inherent losses is likely to be greater or less than that suggested by historical experience. In normal circumstances, historical experience provides the most objective and relevant information from which to assess inherent loss within each portfolio, though sometimes it provides less relevant information about the inherent loss in a given portfolio at the balance sheet date, for example, when there have been changes in economic, regulatory or behavioural conditions which result in the most recent trends in portfolio risk factors being not fully reflected in the statistical models. In these circumstances, the risk factors are taken into account by adjusting the impairment allowances derived solely from historical loss experience.

Risk factors include loan portfolio growth, product mix, unemployment rates, bankruptcy trends, geographical concentrations, loan product features, economic conditions such as national and local trends in housing markets, the level of interest rates, portfolio seasoning, account management policies and practices, changes in laws and regulations, and other influences on customer payment patterns. Different factors are applied in different regions and countries to reflect local economic conditions, laws and regulations. The methodology and the assumptions used in calculating impairment losses are reviewed regularly in the light of differences between loss estimates and actual loss experience. For example, roll rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure they remain appropriate.

However, the exercise of judgement requires the use of assumptions which are highly subjective and very sensitive to the risk factors, in particular to changes in economic and credit conditions across a large number of geographical areas. Many of the factors have a high degree of interdependency and there is no single factor to which our loan impairment allowances as a whole are sensitive. They are particularly sensitive to general economic and credit conditions in North America, however. For example, a 10% increase in impairment allowances on collectively assessed loans and advances in North America would increase loan impairment allowances by US$0.9bn at 31 December 2010 (2009: US$1.3bn). It is possible that the outcomes within the next financial year could differ from the assumptions built into the models, resulting in a material adjustment to the carrying amount of loans and advances.

Goodwill impairment

Our accounting policy for goodwill is described in Note 2p on the Financial Statements. Note 24 on the Financial Statements lists our cash generating units (CGU s) by geographical region and global business. HSBC s total goodwill amounted to US$22bn at 31 December 2010 (2009: US$23bn).

The review of goodwill impairment reflects management s best estimate of the following factors:

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 necessarily and appropriately reflect management s view of future business prospects at the time of the assessment; and

the rates used to discount future expected cash flows are based on the costs of capital assigned to individual CGUs and can have a significant effect on their valuation. 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 inherent risk of the business being evaluated. These variables are subject to fluctuations in external market rates and economic conditions beyond our control and therefore require the exercise of significant judgement and are consequently subject to uncertainty.

A decline in a CGU s expected cash flows and/or an increase in its cost of capital reduces the CGU s estimated recoverable amount. If this is lower than the carrying value of the CGU, a charge for impairment of goodwill is recognised in our income statement for the year.

The accuracy of forecast cash flows is subject to a high degree of uncertainty in volatile market conditions. In such market conditions, management retests goodwill for impairment more frequently than annually to ensure 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.

During 2010, no impairment of goodwill was identified (2009: nil). In addition to the annual impairment test which was performed as at 1 July 2010, management reviewed the current and expected performance of the CGUs as at 31 December 2010 and determined that there was no indication of potential impairment of the goodwill allocated to them. However, in the event of a significant deterioration in economic and credit conditions compared with those reflected by management in the cash flow forecasts for the CGUs, a material adjustment to a CGU s recoverable amount may occur which may result in the recognition of an impairment charge in the income statement.

Note 24 on the Financial Statements includes details of the CGU s with significant balances of goodwill, states the key assumptions used to assess the goodwill in each of those CGUs for impairment and provides a discussion of the sensitivity of the carrying value of goodwill to changes in key assumptions.

Valuation of financial instruments

Our accounting policy for determining the fair value of financial instruments is described in Note 2d on the Financial Statements.

The best evidence of fair value is a quoted price in an actively traded market. In the event that the market for a financial instrument is not active, a valuation technique is used. The majority of valuation techniques employ only observable market data and so the reliability of the fair value measurement is high. However, certain financial instruments are valued on the basis of valuation techniques that feature one or more significant market inputs that are unobservable. Valuation techniques that rely to a greater extent on unobservable inputs require a higher level of management judgement to calculate a fair value than those based wholly on observable inputs.

Valuation techniques used to calculate fair values are discussed in Note 16 on the Financial Statements. The main assumptions and estimates which management consider when applying a model with valuation techniques are:

- the likelihood and expected timing of future cash flows on the instrument. These cash flows are usually governed by the terms of the instrument, although judgement may be required when the ability of the counterparty to service the instrument in accordance with the contractual terms is in doubt. Future cash flows may be sensitive to changes in market rates;

selecting an appropriate discount rate for the instrument. The determination of this rate is based on an assessment of what a market participant would regard as the appropriate spread of the rate for the instrument over the appropriate risk-free rate; and

judgement to determine what model to use to calculate fair value in areas where the choice of valuation model is particularly subjective, for example, when valuing complex derivative products.

When applying a model with unobservable inputs, estimates are made to reflect uncertainties in fair values resulting from a lack of market data inputs, for example, as a result of illiquidity in the market. For these instruments, the fair value measurement is less reliable. Inputs into valuations based on unobservable data are inherently uncertain because there is little or no current market data available from which to determine the level at which an arm s length transaction would occur under normal business conditions. However, in most cases there is some market data available on which to base a determination of fair value, for example historical data, and the fair values of most financial instruments are based on some market observable inputs even when unobservable inputs are significant.

The value of financial assets and liabilities measured at fair value using a valuation technique was US$599bn (2009: US$599bn) and US$499bn (2009: US$447bn), respectively or 56% (2009: 56%) of total financial assets and 77% (2009: 75%) of total financial liabilities measured at fair value.

Disclosures of the types and amounts of adjustments made in determining the fair value of financial instruments measured at fair value using valuation techniques, and a sensitivity analysis of fair values for financial instruments with significant unobservable inputs to reasonably possible alternative assumptions can be found in Note 16 on the Financial Statements. Given the uncertainty and subjective nature of valuing financial instruments at fair value, it is possible that the outcomes in the next financial year could differ from the assumptions used, and this could result in a material adjustment to the carrying amount of financial instruments measured at fair value.

Impairment of available-for-sale financial assets

Our accounting policy for impairment of available-for-sale financial assets is described in Note 2j on the Financial Statements.

At 31 December 2010, our total available-for-sale financial assets amounted to US$381bn (2009: US$352bn), of which US$373bn or 98% (2009: US$342bn; 97%) were debt securities. The available-for-sale fair value reserve relating to debt securities amounted to a deficit of US$6.2bn (2009: deficit of US$11.4bn). A deficit in the available-for-sale fair value reserve occurs on debt securities when the fair value of a relevant security is less than its acquisition cost (net of any principal repayments and amortisation) after deducting any previous impairment loss recognised in the income statement, but where there is no evidence of any impairment or, if an impairment was previously recognised, any subsequent impairment.

Management is required to exercise judgement in determining whether there is objective evidence that an impairment loss has occurred. Once an impairment has been identified, the amount of impairment loss is measured with reference to the fair value of the asset. More information on assumptions and estimates requiring management judgement relating to the determination of fair values of financial instruments is provided above in Valuation of financial instruments .

Deciding whether an available-for-sale debt security is impaired requires objective evidence of both the occurrence of a loss event and a related decrease in estimated future cash flows. The degree of judgement involved is less when cash flows are readily determinable, but increases when estimating future cash flows requires consideration of a number of variables, some of which may be unobservable in current market conditions.

There is no single factor to which the Group s charge for impairment of available-for-sale debt securities is particularly sensitive, because of the various types of securities we hold, the range of geographical areas in which those securities are held, and the wide range of factors which can affect the occurrence of loss events and the cash flows of securities, including different types of collateral.

The most significant judgements concern more complex instruments, such as ABSs, where it is necessary to consider factors such as the estimated future cash flows on underlying pools of collateral including prepayment speeds, the extent and depth of market price declines and changes in credit ratings. The review of estimated future cash flows on underlying collateral is subject to uncertainties when the assessment is based on historical information on pools of assets, and judgement is required to determine whether historical performance remains representative of current economic and credit conditions.

Further details of the nature and extent of our exposures to ABSs classified as available-for-sale and a more detailed description of the assumptions and estimates used in assessing these securities for impairment, together with a discussion of those assets which are most sensitive to possible future impairment, are provided in Securitisation exposures and other structured products on page 128.

It is possible that outcomes in the next financial year could be different from those modelled when seeking to identify impairment on available-for-sale debt securities. In this event, impairment may be identified in available-for-sale debt securities which had previously been determined not to be impaired, potentially resulting in the recognition of material impairment losses in the next financial year.

Deferred tax assets

Our accounting policy for the recognition of deferred tax assets is described in Note 2s on the Financial Statements. The recognition of a deferred tax asset relies on an assessment of the probability and sufficiency of future taxable profits, future reversals of existing taxable temporary differences and ongoing tax planning strategies.

The most significant judgements concern the US deferred tax assets, given the recent history of losses in our US operations. Net US deferred tax assets amounted to US$4bn or 58% (2009: US$5.1bn; 59%) of deferred tax assets recognised on the Group s balance sheet.

Recognition of US deferred tax assets is based on the evidence available about conditions at the balance sheet date, and requires significant judgements to be made regarding projections of loan impairment charges and the timing of recovery in the US economy. These judgements take into consideration the effect of both positive and negative evidence, including historical financial performance, projections of future taxable income, future reversals of existing taxable temporary differences, tax planning strategies and the availability of loss carrybacks.

Projections of future taxable income in the US are based on business plans, future capital requirements and ongoing tax planning strategies. These projections include assumptions about future house prices, US economic conditions, including unemployment levels and their impact on loan impairment charges, and capital support from HSBC Holdings. These forecasts are consistent with the assumption that it is probable that the results of future operations will generate sufficient taxable income to support the deferred tax assets. In management s judgement, recent market conditions, which have resulted in losses being incurred in the US, will create significant downward pressure and volatility regarding the profit or loss before tax in the next few years. To reflect this, the assessment of recoverability of the deferred tax assets in the US significantly discounts any future expected taxable income and relies to a greater extent on capital support to the US operations from HSBC Holdings, including tax planning strategies implemented in relation to such support.

The most significant tax planning strategy is the investment of capital in our US operations to ensure the realisation of the deferred tax assets. The transfer of a subsidiary as part of an internal reorganisation on 31 January 2010 provided substantial support for the recoverability of the US deferred tax assets. Management expects that, with support, our US operations will continue to execute their business strategies and plans until they return to profitability. If HSBC Holdings were to decide not to provide ongoing support, the full recovery of the deferred tax asset may no longer be probable and could result in a significant reduction of the deferred tax asset which would be recognised as a charge in the income statement.

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Customer groups and global businesses

Basis of preparation

The results are presented in accordance with the accounting policies used in the preparation of HSBC s consolidated financial statements. Our operations are closely integrated and, accordingly, the presentation of customer group and global business data includes internal allocations of certain items of income and expense. These allocations include the costs of certain support services and GMO functions, to the extent that these 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.

Where relevant, income and expense amounts presented include the results of inter-segment funding as well as inter-company and inter-business line transactions. All such transactions are undertaken on arm s length terms.

Summary

HSBC s senior management reviews operating activity on a number of bases, including by geographical region and by customer group and global business. Capital resources are allocated and performance is assessed primarily by geographical region, as presented on page 50.

The commentaries below present customer groups and global businesses followed by geographical regions. Performance is discussed in this order because certain strategic themes, business initiatives and trends affect more than one geographical region. All commentaries are on an underlying basis (see page 14) unless stated otherwise. All references to HSBC Finance and HSBC Bank USA are also on a management basis as loans referred to HSBC Bank USA from HSBC Finance are managed by the latter and all costs and benefits accrue thereto.

Profit/(loss) before tax

	2010		2009		2008	
	US$m	**%**	US$m	%	US$m	%
Personal Financial Services	**3,518**	**18.5**	(2,065)	(29.2)	(10,974)	(117.9)
Commercial Banking	**6,090**	**32.0**	4,275	60.4	7,194	77.3
Global Banking and Markets	**9,536**	**50.1**	10,481	148.1	3,483	37.4
Global Private Banking	**1,054**	**5.5**	1,108	15.6	1,447	15.6
Other[44]	**(1,161)**	**(6.1)**	(6,720)	(94.9)	8,157	87.6
	19,037	**100.0**	7,079	100.0	9,307	100.0

Total assets[45]

	At 31 December			
	2010		2009	
	US$m	**%**	US$m	%
Personal Financial Services	**527,698**	**21.5**	554,074	23.4
Commercial Banking	**296,797**	**12.1**	251,143	10.6
Global Banking and Markets	**1,758,315**	**71.6**	1,683,672	71.2
Global Private Banking	**116,846**	**4.8**	116,148	4.9
Other	**161,458**	**6.6**	150,983	6.4
Intra-HSBC items	**(406,425)**	**(16.6)**	(391,568)	(16.5)
	2,454,689	**100.0**	2,364,452	100.0

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Products and services

Products and services

Personal Financial Services

PFS offers its products and services to customers based on their individual needs. Premier and Advance services are targeted at mass affluent and emerging affluent customers who value international connectivity and benefit from our global reach and scale. For customers who have simpler everyday banking needs, we offer a full range of banking products and services reflecting local requirements.

In addition, we are one of the largest card issuers in the world, offering HSBC branded cards, co-branded cards with selected partners and private label (store) cards.

Typically, customer offerings include personal banking products (current and savings accounts, mortgages and personal loans, credit cards, debit cards and local and international payment services) and wealth management services (insurance and investment products and financial planning services).

HSBC Premier provides preferential banking services and global recognition to our high net worth customers and their immediate families with a dedicated relationship manager, specialist wealth advice and tailored solutions. Customers can access emergency travel assistance, priority telephone banking and an online global view of their Premier accounts around the world with free money transfers between them.

HSBC Advance provides a range of preferential products and services customised to meet local needs. With a dedicated telephone service, access to wealth advice and online tools to support financial planning, it gives customers an online global view of their Advance accounts with money transfers between them.

Wealth Solutions & Financial Planning: a financial planning process designed around individual customer needs to help our clients to protect, grow and manage their wealth through best-in-class investment and wealth insurance products manufactured by in-house partners (Global Asset Management, Global Markets and HSBC Insurance) and by selected third party providers.

Customers can transact with the bank via a range of channels such as internet banking and self-service terminals in addition to traditional and automated branches and telephone service centres.

Commercial Banking

We segment our CMB business into Corporate, to serve both Corporate and Mid-Market companies with more sophisticated financial needs and Business Banking, to serve the small and medium-sized enterprises (SME s) sector. This enables the development of tailored customer propositions while adopting a broader view of the entire commercial banking sector, from sole

Financing: we offer a broad range of financing, both domestic and cross-border, including overdrafts, receivables finance, term loans and syndicated, leveraged, acquisition and project finance. Asset finance is offered in selected sites, focused on leasing and instalment finance for vehicles, plant and equipment.

Payments and cash management: we are a leading provider of domestic and cross-border payments and collections, liquidity management and account proprietors to large corporations. This allows us to provide continuous support to companies as they expand both domestically and internationally, and ensures a clear focus on the business banking segments, which are typically the key to innovation and growth in market economies.

We place particular emphasis on international connectivity to meet our business customers needs and aim to be recognised as the leading international bank in all our markets and the best bank for business in our largest markets.

services worldwide, delivered through our e-platform, HSBC net.

International trade: we provide various international trade products and services, to both buyers and suppliers such as export finance, guarantees, documentary collections and forfeiting to improve efficiency and help mitigate risk throughout the supply chain.

Treasury: CMB customers are volume users of our foreign exchange, derivatives and structured products.

Capital markets & advisory: capital raising on debt and equity markets and advisory services are available as required.

Commercial cards: card issuing helps customers enhance cash management, credit control and purchasing. Card acquiring services enable merchants to accept credit and debit card payments in person or remotely.

Insurance: CMB offers key person, employee benefits and a variety of commercial risk insurance such as property, cargo and trade credit.

Direct channels: these include online and direct banking offerings such as telephone banking, HSBCnet and Business Internet Banking.

Global Banking and Markets

GB&M provides tailored financial solutions to major government, corporate and institutional clients and private investors worldwide. Managed as a global business, GB&M operates a long-term relationship management approach to build a full understanding of clients financial requirements. Sector-focused client service teams comprising relationship managers and product specialists develop financial solutions to meet individual client needs. With dedicated offices in over 65 countries and access to HSBC s worldwide presence and capabilities, this business serves subsidiaries and offices of our clients on a global basis.

GB&M is managed as four principal business lines: Global Markets, Global Banking, Global Asset Management and Principal Investments. This structure allows us to focus on relationships and sectors that best fit the Group s footprint and facilitate seamless delivery of our products and services to clients.

Global Markets operations consist of treasury and capital markets services. Products include foreign exchange; currency, interest rate, bond, credit, equity and other derivatives; government and non-government fixed income and money market instruments; precious metals and exchange-traded futures; equity services; distribution of capital markets instruments; and securities services, including custody and clearing services and funds administration to both domestic and cross-border investors.

Global Banking offers financing, advisory and transaction services. Products include:

capital raising, advisory services, bilateral and syndicated lending, leveraged and acquisition finance, structured and project finance, lease finance and non-retail deposit taking;

international, regional and domestic payments and cash management services; and trade services for large corporate clients.

Global Asset Management offers investment solutions to institutions, financial intermediaries and individual investors globally.

Principal Investments includes our strategic relationships with third-party private equity managers and other investments.

Global Private Banking

HSBC Private Bank is the principal marketing name of our international private banking business, Global Private Banking (GPB). Utilising the most suitable products from the marketplace, GPB works with its clients to offer both traditional and innovative ways to manage and preserve wealth while optimising returns.

GPB accesses expertise in six major advisory centres in Hong Kong, Singapore, Geneva, New York, Paris and London to identify opportunities which meet clients needs and investment strategies.

Private Banking services comprise multi-currency deposit accounts and fiduciary deposits, credit and specialist lending, treasury trading services, cash management, securities custody and clearing. GPB works to ensure that its clients have full access to other products and services available in HSBC such as credit cards, internet banking, corporate banking and investment banking.

Private Wealth Management comprises both advisory and discretionary investment services. A wide range of investment vehicles is covered, including bonds, equities, derivatives, options, futures, structured products, mutual funds and alternatives (hedge funds, private equity and real estate).

Corporate Finance Solutions helps provide clients with cross border solutions for their companies, working in conjunction with GB&M.

Private Wealth Solutions comprise inheritance planning, trustee and other fiduciary services designed to protect wealth and preserve it for future generations through structures tailored to meet the individual needs of each family. Areas of expertise include trusts, foundation and company administration, charitable trusts and foundations, insurance, family office advisory and philanthropy.

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Personal Financial Services

PFS provides 92 million individual and self-employed customers with financial services in over 60 markets worldwide.

	2010 US$m	2009 US$m	2008 US$m
Net interest income	**24,161**	25,107	29,419
Net fee income	**7,336**	8,238	10,107
Other income	**1,079**	2,070	1,963
Net operating income[46]	**32,576**	35,415	41,489
Impairment charges[47]	**(11,259)**	(19,902)	(21,220)
Net operating income	**21,317**	15,513	20,269
Total operating expenses	**(18,805)**	(18,292)	(31,704)
Operating profit/(loss)	**2,512**	(2,779)	(11,435)
Income from associates[48]	**1,006**	714	461
Profit/(loss) before tax	**3,518**	(2,065)	(10,974)

Return to profitability in PFS as credit quality improved

HSBC Advance launched in 34 markets in its first year

Significant increase in mortgage lending in Hong Kong and the UK

Strategic direction

Our strategy for PFS is to use our global reach and scale to grow profitably in selected markets by providing relationship banking and wealth management services. PFS employs two globally consistent propositions in Premier and Advance and focuses on deepening customer relationships and increasing the penetration of wealth management services. In markets where we already have scale or where scale can be built over time, we provide services to all customer segments. In other markets, we participate more selectively, targeting mass affluent customers which have strong international connectivity or where our global scale is crucial.

For footnotes, see page 83.

Review of performance

PFS reported a profit before tax of US$3.5bn compared with a reported and underlying loss of US$2.1bn in 2009. This was largely attributable to a decline in loan impairment charges in the US and the managed reduction of certain higher risk portfolios in Latin America, Asia and the Middle East. Performance improved in all regions as the credit quality of our lending portfolios generally rose and revenue grew in Asia and Europe, reflecting higher investment-related income, increased insurance revenue in Hong Kong and mortgage lending growth combined with wider spreads in the UK. Income from associates, particularly Ping An Insurance, increased, driven by strong sales growth.

Revenue fell, largely in HSBC Finance, due to lower lending balances in both the run-off portfolio and in the Card and Retail Services business. Card fees also decreased in North America following the implementation of the CARD Act. Revenue was further affected by an adverse fair value movement related to the non-qualifying hedges recorded in HSBC Finance compared with a favourable movement in 2009, as long-term interest rates declined.

We continued to invest in our business by hiring new relationship managers, investing in systems and infrastructure and developing our product offerings. Operating expenses remained broadly unchanged as a rise in costs in Asia from increased headcount and higher marketing expenditure in support of business expansion was broadly offset by strict cost control across the Group and lower costs associated with the reduced scope of the business in the US.

Loan impairment charges and other credit risk provisions fell by 44% in the improved economic conditions, reflecting a decline in lending balances, enhanced collection processes and tighter lending criteria. The decline in lending was significant in the US as the run-off of the non-core portfolio continued and balances fell in the Card and Retail Services business, where there were fewer active accounts and customers reduced their credit card debt. In addition, certain higher risk portfolios in Latin America, Asia and the Middle East were managed down and repositioned to higher quality assets, resulting in an improvement in credit quality.

In the UK, we increased our market share of mortgage lending, while maintaining a conservative loan to value ratio on new business. We grew mortgage lending in Asia, significantly in Hong Kong, where the introduction of HIBOR-linked mortgages drove volume growth and enabled us to maintain our market leadership. In Australia, Singapore and Malaysia we were able to grow mortgage volumes through targeted marketing campaigns. Customer account balances also grew, largely on the back of increased customer numbers in Asia and the UK.

HSBC Premier, our flagship global customer proposition, was available in 47 markets and had grown to 4.4m customers at the end of 2010. We attracted over 980,000 net new customers in 2010, of whom over 50% were new to HSBC.

We made further progress in standardising our various offerings across the Group for emerging mass affluent customers with the continued transition of eligible customers to HSBC Advance, our second globally consistent proposition. At 31 December 2010, Advance had a customer base of 4.6m and was available in 34 markets. During 2010, HSBC s Global View and Global Transfer online capabilities were extended to our Advance customer base. These services allow Premier and Advance customers to access and manage all their accounts through one single logon and transfer funds between their overseas accounts online. Both the volume and the value of transfers increased strongly during the year as our target customer base and general awareness of these services grew.

Our World Selection global investment offering continued to grow and is now available in 26 markets with total assets under management of US$7.2bn at 31 December 2010.

We further enhanced our services and made banking easier for our customers with initiatives such as increased Saturday branch opening in the UK, the launch of retail renminbi wealth management products, mobile banking and online real time bond trading in Hong Kong, and the upgrading of the US automatic teller machine (ATM) network to accept deposits.

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Commercial Banking

CMB offers a full range of commercial financial services and tailored propositions to 3.6m customers ranging from sole proprietors to publicly quoted companies in 65 countries.

	2010 US$m	2009 US$m	2008 US$m
Net interest income	**8,487**	7,883	9,494
Net fee income	**3,964**	3,702	4,097
Other income	**1,383**	1,268	1,726
Net operating income[46]	**13,834**	12,853	15,317
Impairment charges[47]	**(1,805)**	(3,282)	(2,173)
Net operating income	**12,029**	9,571	13,144
Total operating expenses	**(6,831)**	(5,963)	(6,581)
Operating profit	**5,198**	3,608	6,563
Income from associates[48]	**892**	667	631
Profit before tax	**6,090**	4,275	7,194

Strong balance sheet growth with 21% rise in lending to US$239bn

Significant-pre-tax profit contribution from emerging markets at 67%

First international bank to complete renminbi trade settlements across six continents

Strategic direction

CMB s core strategy is focused on two key initiatives:

- to be the leading international business bank in all our markets, leveraging HSBC s extensive geographical network together with its product expertise in payments, trade, receivables finance and foreign exchange to actively support customers who are trading and investing internationally; and

to be the best bank for small- and medium-sized enterprises in our largest markets.

For footnotes, see page 83.

Review of performance

In 2010, CMB reported profit before tax of US$6.1bn, 42% higher than in 2009 with growth across all regions. Excluding the gains from the sales in 2010 of HSBC Insurance Brokers and our stake in the Wells Fargo HSBC Trade Bank, and similar non-recurring items in 2009, (see page 14), profit before tax increased by 48%. The rise in profit reflected an improvement in the credit environment and strong growth in world trade.

Revenue grew by 8% to US$13.7bn, mainly in Asia, where we expanded customer lending significantly and increased our fee income from remittances, trade and investments. Our insurance operations also performed strongly in Asia, with an increased uptake of our life insurance products in Hong Kong. In North America, repricing initiatives led to a notable increase in revenue.

Loan impairment charges and other credit risk provisions declined by 46% to US$1.8bn with favourable variances in all regions as the credit environment improved and our exposure to higher risk portfolios was managed down.

Excluding CMB s share of the non-recurring accounting gains related to the change in the UK pension scheme, (see page 26), operating expenses increased by 11% to US$6.8bn as we continued to invest for future revenue growth in those markets that we see as central to international connectivity. We hired more relationship managers in France, Brazil, Mexico and Hong Kong, and continued to invest in systems to improve our customer experience. As a result, our cost efficiency ratio rose to 49.8% in 2010.

CMB s share of income from associates grew by 33% to US$892m, notably in mainland China.

Customer lending balances rose by 21% to US$239bn, driven by increased demand in Asia as market sentiment improved, and growth in key developed markets such as France and the UK, where we actively supported corporates and SMEs in response to changes in the economy. Our corporate segment increased lending by 25% to US$183bn, notably in Hong Kong and mainland China.

CMB attracted over half a million new customers in 2010, taking the total to 3.6m, and we grew customer account balances by 8%, with significant growth in Asia where HSBC was ranked as the best cash management bank in 2010 by *Euromoney*.

In line with our strategy to be the leading international business bank, we continued to pursue opportunities to expand our customer base of businesses that trade and invest internationally. In 2010, we opened CMB s first corporate branch in Switzerland to enable our Swiss-based customers to access our international banking services, particularly in faster growing markets. In the UK, we recruited 139 new International Commercial Managers to support the international expansion plans of UK businesses.

Our geographical presence across both developed and emerging markets allowed us to capitalise on the rising levels of international trade flows, notably in Asia and Europe, where we gained export market share in 2010. In the Middle East, we increased our lending to exporters in the region by 69%. In the United Arab Emirates (UAE) specifically, our average lending to exporters more than doubled in 2010 to US$700m.

The number of successful cross-border referrals increased by 77% compared with 2009, with a total transaction value in 2010 of almost US$15bn. Significantly, successful intra-Asia referrals doubled from 2009, while referrals from mainland China more than doubled reflecting the increased appetite of Chinese business to explore international opportunities.

CMB continued to demonstrate connectivity with other customer groups within HSBC. Our partnership with GB&M allowed us to support our customers in accessing capital markets to help them grow and expand internationally. Successful referrals from CMB represented 51% of total net new money generated from internal referrals to GPB in 2010, while 5% of new Premier accounts were referred from CMB.

CMB has a diverse suite of products to support businesses that trade internationally. We are the second largest export factor globally and, in
2010, we launched our Receivables Finance proposition in Germany, Europe s largest economy, which has rapidly growing export ties with Asia. In the UK, we increased international trade finance by 13%. In addition, we successfully piloted the Supplier Invoice Finance Scheme, a reverse factoring product, in India, mainland China and Hong Kong.

We became the first international bank to provide renminbi-denominated trade settlements across six continents in 2010 and we are one of the largest international banks in Hong Kong to offer renminbi products, with total transactions exceeding US$6.7bn in 2010.

Our Business Banking propositions are focused on better serving SMEs, especially those that trade internationally. At the end of 2010, we had over 3.4m customers worldwide in the Business Banking segment, representing 55% of CMB s total deposit balances and providing an important source of funding for our Corporate segment.

We continue to recognise the importance of SMEs to sustained economic recovery and provided working capital finance for this sector throughout 2010. In Hong Kong, we maintained our active participation in the Government Special Loan Guarantee Scheme, through which we provided US$1.5bn in SME financing in 2010. In the UK, we increased new lending to SMEs by 19% in 2010, opened accounts for over 125,000 customers starting new businesses and added over 170 extra local business managers.

We continued to develop and improve our direct channels through enhanced telephone-based relationship management services in key markets, including the launch of smartphone services in Hong Kong. In the UK, we also launched straight-through foreign exchange services. Notably, we are now the leading direct bank in Europe with over one million SME business customers using our Business Internet Banking platform.

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Global Banking and Markets

GB&M is a global business which provides tailored financial solutions to major government, corporate and institutional clients worldwide.

	2010 US$m	2009 US$m	2008 US$m
Net interest income	**7,348**	8,610	8,541
Net fee income	**4,725**	4,363	4,291
Net trading income[49]	**5,831**	6,875	481
Other income	**2,043**	1,972	205
Net operating income[46]	**19,947**	21,820	13,518
Impairment charges[47]	**(990)**	(3,168)	(1,471)
Net operating income	**18,957**	18,652	12,047
Total operating expenses	**(9,962)**	(8,537)	(9,092)
Operating profit	**8,995**	10,115	2,955
Income from associates[48]	**541**	366	528
Profit before tax	**9,536**	10,481	3,483

Employee expenses (including payroll and bonus taxes) in operating expenses US$4,737m

(2009: US$4,335m: 2008: US$4,263m)

Strong contribution from emerging markets

Best Global Emerging Markets Bank

Best Global Emerging Markets Debt House

Emerging Markets Bond House of the Year

Best Debt House in Asia	*International Financing Review Awards 2010*
Euromoney Awards for Excellence 2010	

Strategic direction

In 2010, GB&M continued to pursue its now well-established emerging markets-led and financing-focused strategy, encompassing HSBC s objective to be a leading wholesale bank by:

- utilising the Group s extensive distribution network;
- developing GB&M s hub-and-spoke business model; and
- continuing to build capabilities in major hubs to support the delivery of an advanced suite of services to major government, corporate and institutional clients across the HSBC network.

This combination of product depth and distribution strength is fundamental to meeting the needs of existing and new clients and allowing GB&M to achieve its strategic goals.

For footnotes, see page 83.

Review of performance

GB&M reported profit before tax of US$9.5bn, 9% lower than in 2009. On an underlying basis, which excludes the gains resulting from the sale of Eversholt Rail Group and HSBC Private Equity (Asia) Ltd in 2010, profit before tax declined by 14%, driven by lower income from Balance Sheet Management and Credit and Rates trading and higher operating costs. Profitability benefited from a significant reduction in loan impairment charges and other credit risk provisions. Operating results remained well diversified across our businesses with a strong contribution from emerging markets, where we continued to support existing and anticipated new business, including introducing a China desk in the Middle East and a Latam desk in Hong Kong.

Net operating income before loan impairment charges and other credit risk provisions decreased by 11%, mainly due to lower net interest income in Balance Sheet Management from the maturing of higher yielding positions, low interest rates and flattening yield curves. Lower trading income largely reflected uncertainty in the eurozone, particularly in the second half of 2010. This was offset in part by a net release of US$429m largely relating to legacy positions in Credit trading and monoline Credit exposures, compared with a reported write-down of US$331m in 2009, following a general improvement in ABS prices. Trading income also benefited from a small favourable fair value movement on structured liabilities, compared with an adverse fair value movement in 2009, resulting in a reported favourable movement of US$466m.

Loan impairment charges and other credit risk provisions decreased by US$2.2bn. A US$1.2bn reduction in loan impairment charges to US$500m was driven by a general improvement in the credit environment and the non-recurrence of significant charges taken in relation to a small number of clients in 2009. Credit risk provisions on the available-for-sale portfolio decreased by US$981m to US$490m, of which US$444m related to ABSs, significantly lower than the US$1.5bn impairment reported in 2009, due to a slowing in the rate of anticipated losses in the underlying collateral pools.

Higher operating expenses in 2010 reflected the one-off payroll and bonus taxes in the UK and France on certain bonuses paid in respect of 2009 totalling US$309m, the non-recurrence of an accounting gain related to a change in the

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Management view of total operating income

	2010 US$m	2009 US$m	2008 US$m
Global Markets[50]	**9,173**	10,364	2,676
Credit	**1,649**	2,330	(5,502)
Rates	**2,052**	2,648	2,033
Foreign Exchange	**2,752**	2,979	3,842
Equities	**755**	641	(64)
Securities Services[51]	**1,511**	1,420	2,116
Asset and Structured Finance	**454**	346	251
Global Banking	**4,621**	4,630	5,718
Financing and Equity Capital Markets	**2,852**	3,070	3,572
Payments and Cash Management[52]	**1,133**	1,053	1,665
Other transaction services[53]	**636**	507	481
Balance Sheet Management[54]	**4,102**	5,390	3,618
Global Asset Management	**1,077**	939	934
Principal Investments	**319**	42	(415)
Other[55]	**655**	455	987
Total operating income	**19,947**	21,820	13,518

Comparative information has been adjusted to reflect the current management view.
For footnotes, see page 83.

delivery of certain staff benefits in the main UK pension scheme in 2009, higher support costs and continued investment in strategic initiatives being undertaken to drive future revenue growth. These included the development of Prime Services and equity market capabilities and the expansion of the Rates and Foreign Exchange e-commerce platforms. The percentage of total reported compensation pool allocated in respect of performance in 2010 to revenues net of loan impairment charges (excluding payroll taxes levied on 2009 bonuses) remained consistent with 2009 on a reported basis.

Global Markets revenues were second only to the results recorded in 2009, demonstrating the continuing strength of our client-facing businesses. Trading income declined, driven by increased competition and reduced margins across core products. Credit and Rates were adversely affected by less favourable market conditions as European sovereign debt concerns resulted in increased economic uncertainty in the eurozone. Foreign Exchange revenues were lower, reflecting spread compression in the more competitive trading environment and a decline in market volatility. Investment in the Equities business, particularly the enhancement of the sales and trading platforms, led to increased market share in our target markets despite lower market volumes and increased competition. Securities Services income grew by 4%, with particularly strong performances in Asia driven by increasing market values and Latin America due to higher interest income. Asset and Structured Finance reported higher revenues from increased deal activity during the year.

Global Banking produced a robust performance as it continued the strategy of focusing on key client relationships to drive market share growth in event-driven and other ancillary businesses. A decrease in revenues from Financing and Equity Capital Markets was due to the adverse effect of continued spread compression. Higher project and export finance revenues were driven by increased deal volumes, while growth in revenue and market share was achieved in the advisory business. Equity Capital Markets revenues fell as total deal values declined due to a reduction in client activity. Despite the adverse effect of the continued low interest rate environment, Payments and Cash Management delivered a 6% increase in revenue driven by strong growth in transaction-driven fee income and customer account balances in Asia.

Revenues in Balance Sheet Management remained high by historical standards but, as expected, declined in 2010 as higher-yielding positions matured and the opportunity for reinvestment was limited by the prevailing low interest rate environment and flatter yield curves.

Robust revenue growth was reported in Global Asset Management. Higher management fee income was recorded across all regions, most notably in our emerging markets businesses. Funds under management (FuM) reached a year-end high of US$439bn at 31 December 2010 of which emerging markets FuM, in countries outside North America, Western Europe, Japan and Australia, were US$145bn. Total FuM grew by 4% compared with 2009, benefiting from positive net inflows of US$16bn and strengthening market performance. New funds launched in the year included the Global High Income Fund and the MultiAlpha Global High Yield Bond Fund.

Principal Investments reported an increase in revenues as improved market conditions resulted in higher gains on sale and a reduction in impairments.

Global Private Banking

GPB works with our high net worth clients to offer both traditional and innovative ways to manage and preserve wealth while optimising returns.

	2010 US$m	2009 US$m	2008 US$m
Net interest income	**1,345**	1,474	1,612
Net fee income	**1,299**	1,236	1,476
Other income	**449**	402	543
Net operating income[46]	**3,093**	3,112	3,631
Impairment (charges)/ recoveries[47]	**12**	(128)	(68)
Net operating income	**3,105**	2,984	3,563
Total operating expenses	**(2,035)**	(1,884)	(2,116)
Operating profit	**1,070**	1,100	1,447
Income from associates[48]	**(16)**	8	
Profit before tax	**1,054**	1,108	1,447

Client assets over 6% up at

US$390bn
2009: US$367bn; 2008: US$352bn

Higher investment in GPB operations in Asia, Latin America and the Middle East

Best Global Wealth Manager
Euromoney Awards for Excellence 2010

Best Private Bank in Asia
Euromoney 2011 Private Banking Survey

Outstanding Private Bank Middle East
Private Banker International Awards 2010

Strategic direction

GPB strives to be the world s leading international private bank, recognised for excellent client experience and global connections.

Our brand, capital strength, extensive global network and positioning provide a strong foundation from which GPB continues to attract and retain clients. Product and service leadership in areas such as alternative investments, foreign exchange, estate planning, credit and investment advice helps us meet the complex international financial needs of individuals and families.

We are well-positioned for sustainable long-term growth through continuing investment in our people, integrated IT solutions and emerging markets-focused domestic operations, along with ensuring our cross-border business meets high standards in the evolving regulatory environment.

For footnotes, see page 83.

Review of performance

Reported profit before tax was US$1.1bn, 5% below 2009 on a reported and an underlying basis, driven by lower net interest income as the persistent low interest rate environment continued to affect deposit spreads and higher operating expenses. Loan impairment charges fell following the non-recurrence of a single specific impairment charge in North America in 2009 and the release of several charges made in previous years as markets recovered.

Net fee income and trading income rose, notably in Asia, as improved client risk appetite led to higher levels of activity, an increase in transaction volumes and positive net inflows of client assets.

Operating expenses increased, reflecting the hiring of front-line staff to cover emerging markets as part of a long-term strategy to further strengthen our international network to better serve clients, along with investment in systems and higher compliance costs resulting from the evolving regulatory environment.

Client assets

	2010	2009
	US$bn	US$bn
At 1 January	**367**	352
Net new money	**13**	(7)
Value change	**13**	27
Exchange and other	**(3)**	(5)
At 31 December	**390**	367

Reported client assets, which include funds under management and cash deposits, increased by US$23bn due to net new money inflows compared with outflows in 2009, and favourable market movements. Net inflows benefited from our strength in emerging markets, newly recruited key relationship managers, and cross-business referrals which generated US$8bn in 2010. This also resulted in an increase in total client assets , the equivalent to many industry definitions of assets under management which includes some non-financial assets held in client trusts, from US$460bn to US$499bn. Investor demand for alternatives, including real estate investments, also attracted strong inflows into HSBC Alternative Investments Limited.

The Family Office Partnership had a number of successes in its first full year, producing a complete range of corporate and personal solutions for top tier clients and strengthening its links with GB&M.

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Other

Other contains the results of certain property transactions, unallocated investment activities, centrally held investment companies, movements in fair value of own debt, HSBC s holding company and financing operations.

	2010 US$m	2009 US$m	2008 US$m
Net interest expense	**(998)**	(1,035)	(956)
Net trading income/ (expense)	**(311)**	279	(530)
Net income/(expense) from financial instruments designated at fair value	**(216)**	(6,443)	7,426
Other income	**6,185**	5,176	6,355
Net operating income/ (expense)[46]	**4,660**	(2,023)	12,295
Impairment (charges)/ recoveries[47]	**3**	(8)	(5)
Net operating income/ (expense)	**4,663**	(2,031)	12,290
Total operating expenses	**(5,918)**	(4,715)	(4,174)
Operating profit/(loss)	**(1,255)**	(6,746)	8,116
Income from associates[48]	**94**	26	41
Profit/(loss) before tax	**(1,161)**	(6,720)	8,157

US$250m

gain on sale and leaseback of Paris and New York headquarters buildings

US$6.5bn

reduction in adverse fair value movements on own debt

Investment in Group Service Centres as migrated activities increase

For footnotes, see page 83.

Notes

Reported loss before tax of US$1.2bn compared with a loss before tax of US$6.7bn in 2009. This included adverse movements of US$63m on the fair value of our own debt attributable to movements in credit spreads in 2010, compared with adverse movements of US$6.5bn in 2009. In addition, 2010 included gains of US$188m following the dilution of our holding in Ping An Insurance and US$62m on the reclassification of Bao Viet to an associate following the purchase of an additional 8% stake. On an underlying basis, the loss before tax increased by US$1.2bn to US$1.3bn. The main items reported under Other , are described in footnote 44 on page 85.

Net trading expense of US$311m compared with income of US$276m in 2009. This change was largely attributable to fair value movements on cross-currency swaps used to economically hedge fixed rate long-term debt issued by HSBC Holdings. The adverse fair value movements of US$304m, which were driven by a decline in long-term US interest rates relative to sterling and euro rates, compared with favourable fair value movements of US$748m on these instruments in 2009. This was partly offset by the non-recurrence of fair value losses arising from the implied contingent forward contract entered into with the underwriters of our rights issue in 2009 and forward foreign exchange contracts associated with the rights issue, which were accounted as derivatives with fair value taken to profit or loss in 2009.

We recognised gains of US$194m and US$56m, respectively, from the sale and leaseback of our headquarters buildings in Paris and New York. These compared with more substantial underlying gains totalling US$667m (US$686m as reported) on the sale and leaseback of 8 Canada Square, London and the sale of a property in Hong Kong in 2009.

Operating expenses rose by 24% to US$5.9bn as an increasing number of operational activities were centralised, notably in the US. These costs were previously incurred directly by customer groups, but are now recorded in Other and charged to customer groups through a recharge mechanism with income reported as Other operating income . In addition, costs at our Group Service Centres rose by 6% as the number of migrated activities increased in line with our Global Resourcing model.

HSBC HOLDINGS PLC
Report of the Directors: Operating and Financial Review (continued)

Reconciliation of reported and underlying profit/(loss) before tax

Personal Financial Services
2010 compared with 2009

	2009 as reported US$m	2009 adjustments[10] US$m	Currency translation[11] US$m	2009 at 2010 exchange rates[12] US$m	2010 as reported US$m	2010 adjustments[10] US$m	2010 underlying US$m	Reported change[13] %	Underlying change[13] %
Net interest income	**25,107**		419	25,526	**24,161**	(8)	24,153	(4)	(5)
Net fee income	**8,238**	(8)	115	8,345	**7,336**	(1)	7,335	(11)	(12)
Other income	**2,070**		101	2,171	**1,079**	(5)	1,074	(48)	(51)
Net operating income[15]	**35,415**	**(8)**	**635**	**36,042**	**32,576**	**(14)**	**32,562**	**(8)**	**(10)**
Loan impairment charges and other credit risk provisions	**(19,902)**		(271)	(20,173)	**(11,259)**		(11,259)	43	44
Net operating income	**15,513**	**(8)**	**364**	**15,869**	**21,317**	**(14)**	**21,303**	**37**	**34**
Operating expenses	**(18,292)**	6	(440)	(18,726)	**(18,805)**	4	(18,801)	(3)	
Operating profit/(loss)	**(2,779)**	**(2)**	**(76)**	**(2,857)**	**2,512**	**(10)**	**2,502**		
Income from associates	**714**		6	720	**1,006**		1,006	41	40
Profit/(loss) before tax	**(2,065)**	**(2)**	**(70)**	**(2,137)**	**3,518**	**(10)**	**3,508**		

2009 compared with 2008

2008

	2008 as reported US$m	2008 adjust-ments[10] US$m	Currency translation[11] US$m	at 2009 exchange rates[16] US$m	2009 as reported US$m	2009 adjust-ments[10] US$m	2009 under-lying US$m	Re-ported change[13] %	Under-lying change[13] %
Net interest income	29,419	(36)	(1,534)	27,849	25,107	(3)	25,104	(15)	(10)
Net fee income	10,107	(32)	(645)	9,430	8,238		8,238	(18)	(13)
Other income	1,963	(121)	(258)	1,584	2,070	(1)	2,069	5	31
Net operating income[15]	41,489	(189)	(2,437)	38,863	35,415	(4)	35,411	(15)	(9)
Loan impairment charges and other credit risk provisions	(21,220)	3	595	(20,622)	(19,902)		(19,902)	6	3
Net operating income	20,269	(186)	(1,842)	18,241	15,513	(4)	15,509	(23)	(15)
Operating expenses (excluding goodwill impairment)	(21,140)	38	1,372	(19,730)	(18,292)	1	(18,291)	13	7
Goodwill impairment	(10,564)			(10,564)				100	100
Operating loss	(11,435)	(148)	(470)	(12,053)	(2,779)	(3)	(2,782)	76	77
Income from associates	461		13	474	714		714	55	51
Loss before tax	(10,974)	(148)	(457)	(11,579)	(2,065)	(3)	(2,068)	81	82

For footnotes, see page 83.

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Report of the Directors: Operating and Financial Review (continued)

Commercial Banking
2010 compared with 2009

	2009 as reported US$m	2009 adjust-ments[10] US$m	Currency translation[11] US$m	2009 at 2010 exchange rates[12] US$m	2010 as reported US$m	2010 adjust-ments[10] US$m	2010 under-lying US$m	Re-ported change[13] %	Under-lying change[13] %
Net interest income	**7,883**	**(1)**	**193**	**8,075**	**8,487**	**(20)**	**8,467**	**8**	**5**
Net fee income	**3,702**	**(164)**	**51**	**3,589**	**3,964**	**(2)**	**3,962**	**7**	**10**
Other income	**1,268**	**(283)**	**12**	**997**	**1,383**	**(124)**	**1,259**	**9**	**26**
Net operating income[15]	**12,853**	**(448)**	**256**	**12,661**	**13,834**	**(146)**	**13,688**	**8**	**8**
Loan impairment charges and other credit risk provisions	**(3,282)**		**(73)**	**(3,355)**	**(1,805)**		**(1,805)**	**45**	**46**
Net operating income	**9,571**	**(448)**	**183**	**9,306**	**12,029**	**(146)**	**11,883**	**26**	**28**
Operating expenses	**(5,963)**	**143**	**(122)**	**(5,942)**	**(6,831)**	**13**	**(6,818)**	**(15)**	**(15)**
Operating profit	**3,608**	**(305)**	**61**	**3,364**	**5,198**	**(133)**	**5,065**	**44**	**51**
Income from associates	**667**	**(1)**	**3**	**669**	**892**		**892**	**34**	**33**
Profit before tax	**4,275**	**(306)**	**64**	**4,033**	**6,090**	**(133)**	**5,957**	**42**	**48**

2009 compared with 2008

	2008 as reported US$m	2008 adjust-ments[10] US$m	Currency translation[11] US$m	2008 at 2009 exchange rates[16] US$m	2009 as reported US$m	2009 adjust-ments[10] US$m	2009 under-lying US$m	Re-ported change[13] %	Under-lying change[13] %

Net interest income	9,494	(29)	(697)	8,768	7,883	(45)	7,838	(17)	(11)
Net fee income	4,097	(26)	(367)	3,704	3,702	(5)	3,697	(10)	
Other income	1,726	(464)	(213)	1,049	1,268	(295)	973	(27)	(7)
Net operating income[15]	15,317	(519)	(1,277)	13,521	12,853	(345)	12,508	(16)	(7)
Loan impairment charges and other credit risk provisions	(2,173)	3	68	(2,102)	(3,282)		(3,282)	(51)	(56)
Net operating income	13,144	(516)	(1,209)	11,419	9,571	(345)	9,226	(27)	(19)
Operating expenses	(6,581)	30	537	(6,014)	(5,963)	27	(5,936)	9	1
Operating profit	6,563	(486)	(672)	5,405	3,608	(318)	3,290	(45)	(39)
Income from associates	631		7	638	667		667	6	5
Profit before tax	7,194	(486)	(665)	6,043	4,275	(318)	3,957	(41)	(35)

For footnotes, see page 83.

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Global Banking and Markets
2010 compared with 2009

	2009 as reported US$m	2009 adjust-ments[10] US$m	Currency translation[11] US$m	2009 at 2010 exchange rates[12] US$m	2010 as reported US$m	2010 adjust-ments[10] US$m	2010 under-lying US$m	Re-ported change[13] %	Under-lying change[13] %
Net interest income	8,610		60	8,670	7,348	(3)	7,345	(15)	(15)
Net fee income	4,363	(38)	20	4,345	4,725		4,725	8	9
Net trading income	6,875		103	6,978	5,831		5,831	(15)	(16)
Other income	1,972			1,972	2,043	(341)	1,702	4	(14)
Net operating income[15]	21,820	(38)	183	21,965	19,947	(344)	19,603	(9)	(11)
Loan impairment charges and other credit risk provisions	(3,168)		13	(3,155)	(990)		(990)	69	69
Net operating income	18,652	(38)	196	18,810	18,957	(344)	18,613	2	(1)
Operating expenses	(8,537)	51	(25)	(8,511)	(9,962)	2	(9,960)	(17)	(17)
Operating profit	10,115	13	171	10,299	8,995	(342)	8,653	(11)	(16)
Income from associates	366		2	368	541		541	48	47
Profit before tax	10,481	13	173	10,667	9,536	(342)	9,194	(9)	(14)

2009 compared with 2008

	2008 as reported US$m	2008 adjust-ments[10] US$m	Currency translation[11] US$m	2008 at 2009 exchange rates[16] US$m	2009 as reported US$m	2009 adjust-ments[10] US$m	2009 under-lying US$m	Re-ported change[13] %	Under-lying change[13] %

Net interest income	8,541	(451)	8,090	8,610	(5)	8,605	1	6
Net fee income	4,291	(267)	4,024	4,363	(1)	4,362	2	8
Net trading income	481	(404)	77	6,875		6,875	1,329	8,829
Other income	205	(151)	54	1,972	(2)	1,970	862	3,548
Net operating income[15]	13,518	(1,273)	12,245	21,820	(8)	21,812	61	78
Loan impairment charges and other credit risk provisions	(1,471)	45	(1,426)	(3,168)		(3,168)	(115)	(122)
Net operating income	12,047	(1,228)	10,819	18,652	(8)	18,644	55	72
Operating expenses	(9,092)	743	(8,349)	(8,537)	3	(8,534)	6	(2)
Operating profit	2,955	(485)	2,470	10,115	(5)	10,110	242	309
Income from associates	528	6	534	366		366	(31)	(31)
Profit before tax	3,483	(479)	3,004	10,481	(5)	10,476	201	249

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HSBC HOLDINGS PLC
Report of the Directors: Operating and Financial Review (continued)

Balance sheet data significant to Global Banking and Markets

	Europe US$m	Hong Kong US$m	Rest of Asia-Pacific US$m	Middle East US$m	North America US$m	Latin America US$m	Total US$m
At 31 December 2010							
Trading assets[71]	**232,918**	**32,023**	**18,256**	**958**	**87,120**	**6,459**	**377,734**
Derivative assets[72]	**199,654**	**21,644**	**17,135**	**832**	**65,153**	**3,955**	**308,373**
Trading liabilities	**178,861**	**8,650**	**3,846**	**122**	**91,980**	**2,702**	**286,161**
Derivative liabilities[72]	**199,751**	**22,622**	**17,121**	**845**	**66,323**	**3,913**	**310,575**
At 31 December 2009							
Trading assets[71]	294,951	25,742	15,960	511	67,466	6,283	410,913
Derivative assets[72]	190,900	16,937	15,660	668	61,192	2,820	288,177
Trading liabilities	169,814	10,720	3,040	13	69,302	2,875	255,764
Derivative liabilities[72]	191,480	16,619	15,500	651	60,178	3,270	287,698
At 31 December 2008							
Trading assets[71]	281,089	45,398	19,192	414	74,498	5,004	425,595
Derivative assets[72]	349,035	34,146	29,124	1,014	156,056	9,618	578,993
Trading liabilities	144,759	13,056	3,633	54	72,325	2,546	236,373
Derivative liabilities[72]	345,970	35,693	29,097	1,016	152,907	9,088	573,771

For footnotes, see page 83.

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Report of the Directors: Operating and Financial Review (continued)

Global Private Banking

2010 compared with 2009

	2009 as reported US$m	2009 adjust-ments[10] US$m	Currency translation[11] US$m	2009 at 2010 exchange rates[12] US$m	2010 as reported US$m	2010 adjust-ments[10] US$m	2010 under-lying US$m	Re-ported change[13] %	Under-lying change[13] %
Net interest income	**1,474**		**(2)**	**1,472**	**1,345**		**1,345**	**(9)**	**(9)**
Net fee income	**1,236**		**(1)**	**1,235**	**1,299**		**1,299**	**5**	**5**
Other income	**402**			**402**	**449**	**1**	**450**	**12**	**12**
Net operating income[15]	**3,112**		**(3)**	**3,109**	**3,093**	**1**	**3,094**	**(1)**	
Loan impairment charges and other credit risk provisions	**(128)**		**1**	**(127)**	**12**		**12**		
Net operating income	**2,984**		**(2)**	**2,982**	**3,105**	**1**	**3,106**	**4**	**4**
Operating expenses	**(1,884)**		**3**	**(1,881)**	**(2,035)**		**(2,035)**	**(8)**	**(8)**
Operating profit	**1,100**		**1**	**1,101**	**1,070**	**1**	**1,071**	**(3)**	**(3)**
Income from associates	**8**			**8**	**(16)**		**(16)**		
Profit before tax	**1,108**		**1**	**1,109**	**1,054**	**1**	**1,055**	**(5)**	**(5)**

2009 compared with 2008

	2008 as reported US$m	2008 adjust-ments[10] US$m	Currency translation[11] US$m	2008 at 2009 exchange rates[16] US$m	2009 as reported US$m	2009 adjust-ments[10] US$m	2009 under-lying US$m	Re-ported change[13] %	Under-lying change[13] %

Net interest income	1,612	(52)	1,560	1,474	1,474	(9)	(6)
Net fee income	1,476	(33)	1,443	1,236	1,236	(16)	(14)
Other income	543	(19)	524	402	402	(26)	(23)
Net operating income[15]	3,631	(104)	3,527	3,112	3,112	(14)	(12)
Loan impairment charges and other credit risk provisions	(68)	2	(66)	(128)	(128)	(88)	(94)
Net operating income	3,563	(102)	3,461	2,984	2,984	(16)	(14)
Operating expenses	(2,116)	54	(2,062)	(1,884)	(1,884)	11	9
Operating profit	1,447	(48)	1,399	1,100	1,100	(24)	(21)
Income from associates				8	8		
Profit before tax	1,447	(48)	1,399	1,108	1,108	(23)	(21)

For footnotes, see page 83.

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Other

2010 compared with 2009

	2009 as reported US$m	2009 adjustments[10] US$m	Currency translation[11] US$m	2009 at 2010 exchange rates[12] US$m	2010 as reported US$m	2010 adjustments[10] US$m	2010 underlying US$m	Reported change[13] %	Underlying change[13] %
Net interest expense	**(1,035)**		**21**	**(1,014)**	**(998)**		**(998)**	**4**	**2**
Net fee income	**125**		**(3)**	**122**	**31**		**31**	**(75)**	**(75)**
Changes in fair value[14]	**(6,533)**	**6,533**			**(63)**	**63**		**99**	
Other income	**5,420**		**29**	**5,449**	**5,690**	**(250)**	**5,440**	**5**	
Net operating income/(expense)[15]	**(2,023)**	**6,533**	**47**	**4,557**	**4,660**	**(187)**	**4,473**		**(2)**
Loan impairment (charges)/recoveries and other credit risk provisions	**(8)**			**(8)**	**3**		**3**		
Net operating income/(expense)	**(2,031)**	**6,533**	**47**	**4,549**	**4,663**	**(187)**	**4,476**		**(2)**
Operating expenses	**(4,715)**		**(50)**	**(4,765)**	**(5,918)**		**(5,918)**	**(26)**	**(24)**
Operating loss	**(6,746)**	**6,533**	**(3)**	**(216)**	**(1,255)**	**(187)**	**(1,442)**	**81**	**(568)**
Income from associates	**26**			**26**	**94**		**94**	**262**	**262**
Loss before tax	**(6,720)**	**6,533**	**(3)**	**(190)**	**(1,161)**	**(187)**	**(1,348)**	**83**	**(609)**

2009 compared with 2008

	2008 as	2008 adjust-	Currency	2008 at 2009 exchange	2009 as	2009 adjust-	2009 under-	Re- ported	Under- lying

	reported	ments[10]	translation[11]	rates[16]	reported	ments[10]	lying	change[13]	change[13]
	US$m	US$m	US$m	US$m	US$m	US$m	US$m	%	%
Net interest expense	(956)		12	(944)	(1,035)		(1,035)	(8)	(10)
Net fee income	53		(3)	50	125		125	136	150
Changes in fair value[14]	6,570	(6,570)			(6,533)	6,533			
Gains on disposal of French regional banks	2,445	(2,445)						(100)	
Other income	4,183	(95)	(13)	4,075	5,420		5,420	30	33
Net operating income/(expense)[15]	12,295	(9,110)	(4)	3,181	(2,023)	6,533	4,510		42
Loan impairment charges and other credit risk provisions	(5)		(1)	(6)	(8)		(8)	(60)	(33)
Net operating income/(expense)	12,290	(9,110)	(5)	3,175	(2,031)	6,533	4,502		42
Operating expenses	(4,174)		70	(4,104)	(4,715)		(4,715)	(13)	(15)
Operating profit/(loss)	8,116	(9,110)	65	(929)	(6,746)	6,533	(213)		77
Income from associates	41		(1)	40	26		26	(37)	(35)
Profit/(loss) before tax	8,157	(9,110)	64	(889)	(6,720)	6,533	(187)		79

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Analysis by customer group and global business

HSBC profit/(loss) before tax and balance sheet data

	2010						
	Personal Financial Services US$m	**Commercial Banking US$m**	**Global Banking & Markets US$m**	**Global Private Banking US$m**	**Other[44] US$m**	**Inter-segment elimination[56] US$m**	**Total US$m**
Profit/(loss) before tax							
Net interest income/(expense)	**24,161**	**8,487**	**7,348**	**1,345**	**(998)**	**(902)**	**39,441**
Net fee income	**7,336**	**3,964**	**4,725**	**1,299**	**31**		**17,355**
Trading income/(expense) excluding net interest income	**(107)**	**427**	**4,327**	**391**	**(358)**		**4,680**
Net interest income on trading activities	**28**	**28**	**1,504**	**21**	**47**	**902**	**2,530**
Net trading income/(expense)[49]	**(79)**	**455**	**5,831**	**412**	**(311)**	**902**	**7,210**
Changes in fair value of long- term debt issued and related derivatives					**(258)**		**(258)**
Net income from other financial instruments designated at fair value	**1,210**	**190**	**36**		**42**		**1,478**
Net income/(expense) from financial instruments designated at fair value	**1,210**	**190**	**36**		**(216)**		**1,220**

Gains less losses from financial investments	**42**	**(1)**	**797**	**(6)**	**136**		**968**
Dividend income	**27**	**12**	**48**	**5**	**20**		**112**
Net earned insurance premiums	**9,737**	**1,379**	**41**		**(11)**		**11,146**
Other operating income	**650**	**585**	**1,147**	**38**	**6,005**	**(5,863)**	**2,562**
Total operating income	**43,084**	**15,071**	**19,973**	**3,093**	**4,656**	**(5,863)**	**80,014**
Net insurance claims[57]	**(10,508)**	**(1,237)**	**(26)**		**4**		**(11,767)**
Net operating income[46]	**32,576**	**13,834**	**19,947**	**3,093**	**4,660**	**(5,863)**	**68,247**
Loan impairment (charges)/recoveries and other credit risk provisions	**(11,259)**	**(1,805)**	**(990)**	**12**	**3**		**(14,039)**
Net operating income	**21,317**	**12,029**	**18,957**	**3,105**	**4,663**	**(5,863)**	**54,208**
Employee expenses[58]	**(5,388)**	**(2,153)**	**(4,735)**	**(1,237)**	**(6,323)**		**(19,836)**
Other operating expenses	**(13,417)**	**(4,678)**	**(5,227)**	**(798)**	**405**	**5,863**	**(17,852)**
Total operating expenses	**(18,805)**	**(6,831)**	**(9,962)**	**(2,035)**	**(5,918)**	**5,863**	**(37,688)**
Operating profit/(loss)	**2,512**	**5,198**	**8,995**	**1,070**	**(1,255)**		**16,520**
Share of profit/(loss) in associates and joint ventures	**1,006**	**892**	**541**	**(16)**	**94**		**2,517**
Profit/(loss) before tax	**3,518**	**6,090**	**9,536**	**1,054**	**(1,161)**		**19,037**
	%	*%*	*%*	*%*	*%*		*%*
Share of HSBC s profit before tax	**18.5**	**32.0**	**50.1**	**5.5**	**(6.1)**		**100.0**
Cost efficiency ratio	**57.7**	**49.4**	**49.9**	**65.8**	**127.0**		**55.2**
Balance sheet data[45]							
	US$m	**US$m**	**US$m**	**US$m**	**US$m**		**US$m**
Loans and advances to customers (net)	**390,957**	**239,286**	**284,503**	**40,665**	**2,955**		**958,366**
Total assets	**527,698**	**296,797**	**1,758,315**	**116,846**	**161,458**	**(406,425)**	**2,454,689**

Customer accounts	**525,184**	**286,007**	**308,453**	**107,130**	**951**	**1,227,725**

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	2009						
	Personal Financial Services US$m	Commercial Banking US$m	Global Banking & Markets US$m	Global Private Banking US$m	Other[44] US$m	Inter-segment elimination[56] US$m	Total US$m
Profit/(loss) before tax							
Net interest income/(expense)	25,107	7,883	8,610	1,474	(1,035)	(1,309)	40,730
Net fee income	8,238	3,702	4,363	1,236	125		17,664
Trading income excluding net interest income	637	332	4,701	322	244		6,236
Net interest income on trading activities	65	22	2,174	22	35	1,309	3,627
Net trading income[49]	702	354	6,875	344	279	1,309	9,863
Changes in fair value of long- term debt issued and related derivatives					(6,247)		(6,247)
Net income/(expense) from other financial instruments designated at fair value	2,339	100	473		(196)		2,716
Net income/(expense) from financial instruments designated at fair value	2,339	100	473		(6,443)		(3,531)
Gains less losses from financial investments	224	23	265	5	3		520
Dividend income	33	8	68	5	12		126
Net earned insurance premiums	9,534	886	54		(3)		10,471

Other operating income	809	739	1,146	48	5,042	(4,996)	2,788
Total operating income/(expense)	46,986	13,695	21,854	3,112	(2,020)	(4,996)	78,631
Net insurance claims[57]	(11,571)	(842)	(34)		(3)		(12,450)
Net operating income/(expense)[46]	35,415	12,853	21,820	3,112	(2,023)	(4,996)	66,181
Loan impairment charges and other credit risk provisions	(19,902)	(3,282)	(3,168)	(128)	(8)		(26,488)
Net operating income/(expense)	15,513	9,571	18,652	2,984	(2,031)	(4,996)	39,693
Employee expenses[58]	(6,069)	(2,072)	(4,335)	(1,198)	(4,790)		(18,464)
Other operating expenses	(12,223)	(3,891)	(4,202)	(686)	75	4,996	(15,931)
Total operating expenses	(18,292)	(5,963)	(8,537)	(1,884)	(4,715)	4,996	(34,395)
Operating profit/(loss)	(2,779)	3,608	10,115	1,100	(6,746)		5,298
Share of profit in associates and joint ventures	714	667	366	8	26		1,781
Profit/(loss) before tax	(2,065)	4,275	10,481	1,108	(6,720)		7,079
	%	%	%	%	%		%
Share of HSBC s profit before tax	(29.2)	60.4	148.1	15.6	(94.9)		100.0
Cost efficiency ratio	51.7	46.4	39.1	60.5	(233.1)		52.0
Balance sheet data[45]							
	US$m	US$m	US$m	US$m	US$m		US$m
Loans and advances to customers (net)	399,460	199,674	256,956	37,031	3,110		896,231
Total assets	554,074	251,143	1,683,672	116,148	150,983	(391,568)	2,364,452
Customer accounts	499,109	267,388	284,727	106,533	1,277		1,159,034

For footnotes, see page 83.

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Profit/(loss) before tax and balance sheet data (continued)

Total				2008			
	Personal Financial Services US$m	Commercial Banking US$m	Global Banking & Markets US$m	Global Private Banking US$m	Other[44] US$m	Inter-segment elimination[56] US$m	Total US$m
Profit/(loss) before tax							
Net interest income/(expense)	29,419	9,494	8,541	1,612	(956)	(5,547)	42,563
Net fee income	10,107	4,097	4,291	1,476	53		20,024
Trading income/(expense) excluding net interest income	175	369	157	408	(262)		847
Net interest income/(expense) on trading activities	79	17	324	14	(268)	5,547	5,713
Net trading income/(expense)[49]	254	386	481	422	(530)	5,547	6,560
Changes in fair value of long- term debt issued and related derivatives					6,679		6,679
Net income/(expense) from other financial instruments designated at fair value	(2,912)	(224)	(438)		747		(2,827)
Net income/(expense) from financial instruments designated at fair value	(2,912)	(224)	(438)		7,426		3,852
	663	193	(327)	64	(396)		197

Gains less losses from financial investments							
Dividend income	90	88	76	8	10		272
Net earned insurance premiums	10,083	679	105		(17)		10,850
Gains on disposal of French regional banks					2,445		2,445
Other operating income	259	939	868	49	4,261	(4,568)	1,808
Total operating income	47,963	15,652	13,597	3,631	12,296	(4,568)	88,571
Net insurance claims[57]	(6,474)	(335)	(79)		(1)		(6,889)
Net operating income[46]	41,489	15,317	13,518	3,631	12,295	(4,568)	81,682
Loan impairment charges and other credit risk provisions	(21,220)	(2,173)	(1,471)	(68)	(5)		(24,937)
Net operating income	20,269	13,144	12,047	3,563	12,290	(4,568)	56,745
Employee expenses[58]	(7,905)	(2,549)	(4,263)	(1,308)	(4,767)		(20,792)
Goodwill impairment	(10,564)						(10,564)
Other operating expenses	(13,235)	(4,032)	(4,829)	(808)	593	4,568	(17,743)
Total operating expenses	(31,704)	(6,581)	(9,092)	(2,116)	(4,174)	4,568	(49,099)
Operating profit/(loss)	(11,435)	6,563	2,955	1,447	8,116		7,646
Share of profit in associates and joint ventures	461	631	528		41		1,661
Profit/(loss) before tax	(10,974)	7,194	3,483	1,447	8,157		9,307
	%	%	%	%	%		%
Share of HSBC s profit before tax	(117.9)	77.3	37.4	15.6	87.6		100.0
Cost efficiency ratio	76.4	43.0	67.3	58.3	33.9		60.1
Balance sheet data[45]							
	US$m	US$m	US$m	US$m	US$m		US$m
Loans and advances to customers (net)	401,402	203,949	287,306	37,590	2,621		932,868

Total assets	527,901	249,218	1,991,852	133,216	145,581	(520,303)	2,527,465
Customer accounts	440,338	235,879	320,386	116,683	2,041		1,115,327

For footnotes, see page 83.

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Geographical regions

Summary

Additional information on results in 2010 may be found in the Financial Summary on pages 14 to 36.

In the analysis of profit by geographical regions that follows, operating income and operating expenses include intra-HSBC items of US$3,125m (2009: US$2,756m; 2008: US$2,492m).

Profit/(loss) before tax

	2010		2009		2008	
	US$m	**%**	US$m	%	US$m	%
Europe	**4,302**	**22.6**	4,009	56.7	10,869	116.7
Hong Kong	**5,692**	**29.9**	5,029	71.0	5,461	58.7
Rest of Asia-Pacific	**5,902**	**31.0**	4,200	59.3	4,722	50.7
Middle East	**892**	**4.7**	455	6.4	1,746	18.8
North America	**454**	**2.4**	(7,738)	(109.3)	(15,528)	(166.8)
Latin America	**1,795**	**9.4**	1,124	15.9	2,037	21.9
	19,037	**100.0**	7,079	100.0	9,307	100.0

Total assets[45]

	At 31 December			
	2010		2009	
	US$m	**%**	US$m	%
Europe	**1,249,527**	**50.9**	1,268,600	53.7
Hong Kong	**429,565**	**17.5**	399,243	16.9
Rest of Asia-Pacific	**278,062**	**11.3**	222,139	9.4
Middle East	**52,757**	**2.1**	48,107	2.0
North America	**492,487**	**20.1**	475,014	20.1
Latin America	**139,938**	**5.7**	115,967	4.9
Intra-HSBC items	**(187,647)**	**(7.6)**	(164,618)	(7.0)
	2,454,689	**100.0**	2,364,452	100.0

Risk-weighted assets[59]

	At 31 December			
	2010		2009	
	US$bn	**%**	US$bn	%
Total	**1,103.1**		1,133.2	
Europe	**301.6**	**27.2**	339.7	29.8
Hong Kong	**106.9**	**9.7**	119.5	10.5
Rest of Asia-Pacific	**217.5**	**19.6**	173.9	15.3
Middle East	**54.1**	**4.9**	54.3	4.8
North America	**330.7**	**29.9**	369.2	32.4
Latin America	**95.9**	**8.7**	81.7	7.2

For footnote, see page 83.

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Europe

Our principal banking operations in Europe are HSBC Bank plc in the UK, HSBC France, HSBC Bank A.S. in Turkey, HSBC Bank Malta p.l.c., HSBC Private Bank (Suisse) S.A. and HSBC Trinkaus & Burkhardt AG. Through these operations we provide a wide range of banking, treasury and financial services to personal, commercial and corporate customers across Europe.

	2010 US$m	2009 US$m	2008 US$m
Net interest income	**11,250**	12,268	9,696
Net fee income	**6,371**	6,267	7,492
Net trading income	**2,863**	5,459	5,357
Other income/(expense)	**2,266**	(450)	8,134
Net operating income[46]	**22,750**	23,544	30,679
Impairment charges[47]	**(3,020)**	(5,568)	(3,754)
Net operating income	**19,730**	17,976	26,925
Total operating expenses	**(15,445)**	(13,988)	(16,072)
Operating profit	**4,285**	3,988	10,853
Income from associates[48]	**17**	21	16
Profit before tax	**4,302**	4,009	10,869
Cost efficiency ratio	**67.9%**	59.4%	52.4%
Year-end staff numbers	**75,698**	76,703	82,093

Reduction in underlying impairment charges[47]
45%

Total UK mortgage market share
5.2%

2009: 4.8%
Strong trade
revenue growth

For footnotes, see page 83.

The commentary on Europe is on an underlying basis unless stated otherwise.

Economic background

After falling by 4.9% in 2009, **UK** Gross Domestic Product (GDP) only partially recovered in 2010, rising 1.4%. This revival in activity was not reflected in a corresponding rise in employment, and the unemployment rate remained at 7.9% in the three months to November. Despite the general economic weakness, the annual rate of Consumer Price Index (CPI) inflation rose during 2010, reaching 3.7% in December, partly because of the rise in value added tax to 17.5% in January, and increases in the price of food and energy following rapid gains in global commodity prices. Wage growth remained subdued, however, with average earnings rising just 2.0% in the year to December. The Bank of England chose to maintain Bank Rate at 0.5% throughout 2010.

The **eurozone** economy also partially recovered during the year, with GDP rising 1.7% in 2010 compared to 2009. The region benefited from the pick-up in the world economy and some improvement in domestic demand. Within the region, Germany recorded the strongest growth rate with its GDP rising 3.5% in the year as a whole. The unemployment rate in the eurozone increased slightly to 10.0% by the end of 2010. The large increases in government debt that emerged in certain parts of the region in recent years began to put upward pressure on government bond yields during 2010, and some governments encountered funding difficulties. In response, a temporary European support fund, the 440bn European Financial Stability Facility was created, and the EU set aside 60bn in a package named the European Financial Stabilisation Mechanism. Greece received a 110bn aid package provided jointly by the International Monetary Fund and eurozone governments. Ireland also drew on international assistance in December. The European Central Bank left its key interest rate at 1.0% throughout the year.

Review of performance

Our European operations reported a pre-tax profit of US$4.3bn, compared with US$4.0bn in 2009, an increase of 7%. In 2010, this included adverse fair value movements of US$198m due to the change in credit spreads on the Group s own debt held at fair value, compared with adverse fair value movements of US$2.8bn in 2009. In addition, we made gains of US$107m on the disposal of the HSBC Insurance Brokers business and US$255m on the sale of Eversholt Rail Group. In 2009, we recorded a gain on the sale of the residual stake in our UK card merchant acquiring business. Excluding these items, underlying pre-tax profits decreased by 35%,

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Profit/(loss) before tax by country within customer groups and global businesses

	Personal Financial Services US$m	Commercial Banking US$m	Global Banking & Markets US$m	Global Private Banking US$m	Other US$m	Total US$m
2010						
UK	**1,223**	**827**	**1,730**	**223**	**(1,605)**	**2,398**
France[60]	**109**	**135**	**405**	**18**	**26**	**693**
Germany		**32**	**267**	**30**	**4**	**333**
Malta	**35**	**56**	**19**			**110**
Switzerland		**(5)**		**265**		**260**
Turkey	**64**	**80**	**105**	**1**		**250**
Other	**(142)**	**80**	**200**	**103**	**17**	**258**
	1,289	**1,205**	**2,726**	**640**	**(1,558)**	**4,302**
2009						
UK	364	1,026	3,045	252	(2,561)	2,126
France[60]	54	102	894	3	(429)	624
Germany		21	255	32	(18)	290
Malta	33	58	9			100
Switzerland			5	448	(3)	450
Turkey	43	97	119	2		261
Other	(182)	(12)	218	117	17	158
	312	1,292	4,545	854	(2,994)	4,009
2008						
UK	1,546	2,361	(469)	250	2,997	6,685
France[60]	139	176	273	10	2,242	2,840
Germany		31	184	32	(22)	225
Malta	59	67	16			142
Switzerland				553		553
Turkey	3	91	130			224
Other	(89)	(4)	61	153	79	200

	1,658	2,722	195	998	5,296	10,869

For footnote, see page 83.

largely due to lower income from GB&M, whose exceptional results of 2009 were not repeated, and an unfavourable year on year movement in certain non-qualifying hedges of US$1.1bn.

GB&M results remained strong by historical standards. However, revenues decreased in 2010 due to less favourable market conditions caused by the impact of the European sovereign debt crisis, particularly in the second half of the year, and lower revenues, as forecast, in Balance Sheet Management.

In PFS, we continued to build long-term relationships through our Premier and Advance offerings, focusing on wealth management and secured lending. We increased our total UK mortgage market share to 5.2%, while maintaining a conservative new lending loan to value ratio of 54%.

In CMB, we made further progress on our strategy of becoming the leading international business bank. We also expanded our business in Germany and launched in Switzerland. In the UK, we increased new lending to SMEs by 19% in 2010.

Net interest income decreased by 7%. Balance Sheet Management revenues declined, as higher-yielding positions matured, interest rates remained low and yield curves flattened in 2010. In Global Banking, tighter spreads in the lending business and lower average lending balances as customers reduced their debt also contributed to the decrease. Customer deposit spreads were adversely affected by the low interest rate environment and competition for deposits. These reductions were offset in part by growth in mortgage lending in the UK and improved asset spreads in both PFS and CMB.

Net fee income increased by 7%, reflecting higher management fees due to an increase in the average value of funds under management, which arose from net inflows and higher market performance. Fees were also received for management services we provided to certain of our Structured Investment Conduits. Partly offsetting these increases were reductions in the levels of debt and equity issuance in the market, compared with the significant volumes seen in 2009.

Net trading income decreased by 47% to US$2.9bn. Less favourable market conditions caused by the impact of the European sovereign debt crisis adversely affected Credit and Rates income. Spread compression from increased competition similarly affected foreign exchange revenues. In addition, net interest income earned on trading activities decreased, driven by reduced holdings of debt securities. These decreases were offset in part by lower net adverse fair value movements on structured liabilities.

Net trading income also included adverse fair value movements of US$304m on non-qualifying hedges used to economically hedge fixed-rate long-term debt issued by HSBC Holdings. These movements were driven by the decline in long-term US dollar interest rates relative to sterling and euro rates in 2010, and compared with favourable fair value movements of US$748m on these instruments in 2009.

Within our legacy Credit book, a net release of previous write-downs on ABSs and monoline exposures as asset prices improved was more than offset by the non-recurrence of gains in other parts of the business.

Net income from financial instruments designated at fair value fell by US$808m. The growth in equity markets in 2010 was lower than in 2009, resulting in lower investment gains recognised on the fair value of assets held to meet liabilities under insurance and investment contracts. To the extent that these gains accrued to policyholders holding unit-linked insurance policies and insurance or investment contracts with DPF, there was a corresponding decrease in Net insurance claims incurred and movement in liabilities to policyholders . In addition, adverse foreign exchange movements were reported in the year on foreign currency debt designated at fair value, issued as part of our overall funding strategy with an offset from trading assets held as economic hedges reported in Net trading income .

Gains less losses from financial investments increased by US$455m as improved market conditions led to gains on sale of private equity investments and lower impairment charges on certain available-for-sale investments.

Net earned insurance premiums were in line with 2009. The decision in 2009 to place our UK motor insurance business into run-off resulted in no new premiums being written in 2010. In addition, a decision was taken during 2010 not to renew certain contracts in the Irish business. By contrast, we generated strong sales activity in the UK life and French insurance businesses.

Other operating income decreased by US$193m because the gain on the sale and leaseback of our Paris headquarters building in 2010 was exceeded by the gain on the sale and leaseback of the Group s London headquarters building in 2009.

Net insurance claims incurred and movement in liabilities to policyholders decreased by 11%. This was driven by lower investment gains compared with 2009 and by the non-recurrence of the strengthening of reserves in 2009 on the now-closed UK motor insurance book which reflected the rising incidence and severity of claims at that time. The decision not to renew certain contracts in the Irish business resulted in a further decrease in claims.

Loan impairment charges and other credit risk provisions decreased by 45% to US$3.0bn, reflecting the more stable credit environment and helped by mitigating actions taken by management. In GB&M, the improved credit outlook, loan restructuring activity, a release of previous collective impairments and lower specific impairment charges in 2010 contributed to a decline in loan impairment charges and other credit risk provisions. Credit risk provisions on certain available-for-sale ABSs also reduced due to a slowing in the rate of anticipated losses in the underlying collateral pools.

In CMB, the reduction in loan impairment charges and other credit risk provisions was largely due to an improvement in the UK property, retail and services sectors, with reductions also seen in our Continental European businesses. The improvement in economic conditions across the region and the effect of low interest rates also resulted in lower delinquencies in the PFS portfolios.

Operating expenses in 2010 included one-off payroll and bonus taxes in the UK and France on certain bonuses paid in respect of 2009 totalling US$324m, primarily in GB&M. Operating expenses in 2009 included an accounting gain of US$480m (US$499m as reported) related to a change in the delivery of certain staff benefits in the main UK pension scheme. Excluding these items, operating expenses were 8% higher than in 2009. This was driven by continued strategic investments in people and infrastructure to support our customers, drive future growth and deliver sustainable long-term reductions in our cost base by re-engineering business processes. In addition, rental expenses increased following the sale and leaseback of our headquarters buildings in London and Paris.

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2009 compared with 2008

Economic background

The **UK** economy suffered a sharp contraction during the course of 2009, although evidence from the final months of the year suggested that some growth had resumed. Gross Domestic Product (GDP) fell by 5% in 2009 the sharpest contraction in over 60 years after a 0.5% increase in 2008. Weakness affected most sectors of the economy, and the unemployment rate hit a 13-year high of 7.9% in July 2009, although some stabilisation of labour market conditions was apparent towards the end of the year. Consumer Price Index (CPI) inflation reached a five-year low of 1.1% in September 2009 before moving towards the Bank of England s 2% target by the end of the year. Nominal house prices appreciated modestly during the second half of 2009, although indicators of housing market activity remained at relatively weak levels. After reducing interest rates to just 0.5% in March 2009, the Bank of England launched the Asset Purchase Facility in an attempt to improve the circulation of credit throughout the economy and support expectations of future economic activity.

The **eurozone** economy also performed poorly during 2009, with GDP falling by 4% following a 0.5% expansion in 2008. Much of this weakness was concentrated in the early months of 2009 and growth resumed in the third quarter, helped by a variety of fiscal stimulus programmes and a rebuilding of inventory levels. Consumer spending proved relatively resilient in early 2009, boosted by a number of purchase incentive schemes, and some weakness was observed as these programmes expired. Unemployment rose to an 11-year high of 10% in December 2009, while CPI temporarily turned negative during the third quarter of the year. The European Central Bank cut interest rates by 150 basis points to finish the year at 1%.

Review of performance

Our European operations reported a pre-tax profit of US$4.0bn, compared with US$10.9bn in 2008. This decline was largely caused by movement in the fair value attributable to credit spread on our own debt. A US$2.8bn expense in 2009 following stabilisation in financial markets and a narrowing of credit spreads largely reversed the US$3.1bn income recognised in 2008, giving a US$5.9bn year on year movement. Also included within these results was a gain on the sale of the residual stake in the UK card merchant acquiring business to Global Payments Inc. of US$280m in June 2009. This followed a
US$425m gain realised in 2008 on the sale of the first tranche. Excluding these gains on sale, the profit on disposal of the French regional banks in July 2008 and the reversal of movements in the fair value of own debt, underlying pre-tax profits grew by US$3.0bn or 83%. This was driven by robust performances in our European GB&M businesses, in particular from the non-recurrence of significant credit-related write-downs taken in 2008 and outstanding results in Rates and Balance Sheet Management. Deterioration in the economic environment and higher unemployment levels led to a rise in loan impairment charges in both PFS and CMB. HSBC Bank continued to provide lending services to its customers while maintaining effective credit control and strengthening collection practices and systems.

Net interest income increased by 43%, with Balance Sheet Management revenues in GB&M rising robustly. This resulted from the early positioning of our balance sheet in anticipation of decisions by central banks to maintain a low base rate environment. Net interest income also benefited from a reduction in the cost of funding trading activities as interest rates fell. Conversely, the PFS and CMB businesses and payments and cash management were adversely affected by continued margin compression following interest rate reductions in late 2008 and early 2009.

Mortgage balances increased as we gained market share in the UK through the success of a new Rate Matcher mortgage promotion and other campaigns launched in line with our secured lending growth strategy. In 2009, our UK bank more than met its commitment to make £15bn (US$24.7bn) of new mortgage lending available to borrowers. In CMB, net lending fell compared with 2008 as a result of muted customer demand. Utilisation of committed overdraft facilities provided by HSBC in the UK to commercial customers was only 40% at the end of 2009, illustrating the potential availability of credit when customer demand resumes. Across most businesses, asset balances declined reflecting reduced customer demand for credit, increased debt issuance as the bond markets reopened in 2009 and our diminished appetite for unsecured lending in Europe. Asset spreads widened, most notably in the UK and Turkey, as funding costs fell in the low interest rate environment and market pricing of corporate lending increased.

Throughout 2009, we worked to retain and build on the personal and commercial banking deposit bases gained in the last quarter of 2008 in the face of fierce competition and the narrowing of spreads across the region following interest rate cuts.

Net fee income fell by 4%. The overall reduction in fees was a consequence of the part-disposal of the UK card merchant acquiring business to a joint venture in 2008 and lower insurance income following the closure of our consumer finance branch network in the UK and reduced sales of discontinued products. In GPB, lower equity brokerage commissions and reduced performance and management fees reflected subdued investor sentiment for risk and structured products; this, together with stock market declines, reduced the average value of funds under management during the year.

We generated higher underwriting fees than in 2008 from increased government and corporate debt issuances, and by taking market share in equity capital markets issues as corporates and financial institutions restructured their balance sheets by raising share capital. As part of our wealth management strategy, we continued to grow our Premier customer base and successfully launched the World Selection fund in the UK which raised US$1.5bn. In France, the Premier customer base grew by over 10% as HSBC brand awareness increased.

Trading income increased by 23% to US$5.5bn due to strong revenues across core businesses. Rates reported a significant increase in income driven by a growth in market share, higher client trading volumes and wider bid-offer spreads. Similarly, revenue in the Credit trading business also rose as credit prices improved and client activity increased with the return of liquidity to the market. Foreign exchange revenue fell, however, reflecting a combination of reduced customer volumes and relatively low market volatility when compared with the exceptional experience of 2008.

Trading income also benefited from significantly lower write-downs on legacy positions in Credit trading, leveraged and acquisition financing and monoline exposures, and from the non-recurrence of a reported US$854m loss in 2008 following the fraud at Madoff Securities. These benefits were partly offset by losses on structured liabilities as credit spreads narrowed (compared with gains in 2008) and a reduction in net interest income on trading activities. This was due to the decline in interest rates, which also contributed to the reduction in the cost of funding trading activities as reported in Net interest income . The tightening of credit spreads also led to a reduction in the carrying value of credit default swap transactions held as hedges in parts of the Global Banking portfolio. In 2008, gains were reported on these credit default swaps following widening credit spreads.

We incurred a net expense of US$1.4bn on *financial instruments designated at fair value,* compared with income in 2008. Gains on the fair value of assets held to meet liabilities under insurance and investment contracts were recognised as equity markets recovered from declines sustained in 2008. To the extent that these gains were attributed to policyholders holding either insurance contracts or investment contracts with DPF, there was a corresponding increase in *net insurance claims incurred and movement in liabilities to policyholders*.

Gains less losses from financial investments were US$192m lower than in 2008 due to the non-recurrence of certain disposals in that year, including MasterCard shares, private equity investments and the remaining stake in the Hermitage Fund.

Net earned insurance premiums decreased by 12%. In the UK demand for the insurance-linked Guaranteed Income Bond fell as we offered more favourable rates on an alternative non-insurance deposit product, giving rise to a US$1.1bn decrease in insurance premium income, with a corresponding decrease in Net insurance claims incurred and movement in liabilities to policyholders . Excluding the effect of a significant re-insurance transaction in 2008 which passed insurance premiums to a third-party reinsurer, net premiums in France increased despite a significant reduction in the distribution network following the disposal of the regional banks in July 2008.

Other operating income increased by 45%, mainly due to a US$576m gain on the sale and leaseback of 8 Canada Square in London which was effected through the disposal of our entire shareholding in the company which was the legal owner of the building and long leasehold interest in 8 Canada Square. In 2008, we reported a gain of US$416m representing the equity deposit on a previously negotiated sale of the building which ultimately did not complete. In addition, a change in mortality assumptions in France resulted in increased PVIF of long-term insurance business. The growth in revenue also reflected the non-recurrence of costs associated with the support of money market funds in the global asset management business in 2008. Offsetting this was the non-recurrence of a favourable embedded value adjustment following the introduction of enhanced benefits to our existing pension products in the UK in 2008, and lower gains on the sale and leaseback of branches.

Net insurance claims incurred and movement in liabilities to policyholders increased by US$2.5bn. The majority of the movement was due to the change in liabilities to policyholders reported above in Financial instruments designated at fair value , and the large one-off reinsurance transaction in France in 2008. In addition, an increase of US$310m in claims reserving was required to reflect a higher incidence and severity of insurance claims in the UK motor underwriting business and a higher incidence of credit protection claims through the reinsurance business in Ireland. Risk mitigation measures implemented in 2009 included the decision to cease originations of UK motor insurance business. This was partly offset by the decrease in liabilities following reduced sales of the personal customer bond product offering noted above.

Loan impairment charges and other credit risk provisions rose by 66% to US$5.6bn as the impact of weaker economic conditions across the region fed through to higher delinquency and default. In GB&M, loan impairment charges and credit risk provisions increased, with the charges concentrated among a small number of clients in the financial and property sectors. The emergence in the year of cash flow impairment on certain asset-backed debt securities held within the available-for-sale portfolios added US$1.1bn to the charge. Impairment booked on these exposures reflects mark-to-market losses which we judge to be significantly in excess of the likely ultimate cash losses.

In CMB, loan impairment charges rose by US$471m, again reflecting the economic downturn. Our commercial property portfolio in the UK
declined during 2009, reflecting our efforts to reduce risk in this sector. In the personal sector, deterioration was most evident in the unsecured portfolios as unemployment rose. As a result of past management action, unsecured lending remained a small proportion of our personal lending portfolio, with the bulk of the portfolio secured in the form of residential mortgages. Despite some increase in losses in the residential sector, impairment charges as a percentage of total lending in this portfolio remained very low at 0.14%.

Operating expenses were held broadly in line with 2008. Excluding an accounting gain of US$499m following a change in the basis of delivering death-in-service, ill health and early retirement benefits for some UK employees, operating expenses increased slightly despite efficiency benefits as higher performance-related awards were made to reflect GB&M s exceptional revenue and profit growth in selective businesses.

In PFS and CMB businesses, operational cost savings reflected the leverage of our global technology platforms and processes to reduce costs and improve customer experience, complemented by tight control over discretionary expenditure and a reduction in staff numbers. Payroll savings and lower Financial Services Compensation Scheme costs were partly offset by an increase in rental costs following the sale and leaseback of properties and higher regular defined benefit pension charges. In Europe, full time equivalent staff numbers fell by some 6,000 during the year.

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Profit/(loss) before tax and balance sheet data Europe

	2010						
	Personal Financial Services US$m	Commercial Banking US$m	Global Banking & Markets US$m	Global Private Banking US$m	Other US$m	Inter-segment elimination[56] US$m	Total US$m
Profit/(loss) before tax							
Net interest income/(expense)	**5,536**	**2,774**	**2,936**	**871**	**(654)**	**(213)**	**11,250**
Net fee income	**2,016**	**1,570**	**1,863**	**883**	**39**		**6,371**
Trading income/(expense) excluding net interest income	**(7)**	**3**	**1,542**	**185**	**(262)**		**1,461**
Net interest income/(expense) on trading activities	**(1)**	**19**	**1,127**	**21**	**23**	**213**	**1,402**
Net trading income/(expense)[49]	**(8)**	**22**	**2,669**	**206**	**(239)**	**213**	**2,863**
Changes in fair value of long-term debt issued and related derivatives					**(365)**		**(365)**
Net income/(expense) from other financial instruments designated at fair value	**496**	**113**	**(23)**		**61**		**647**
Net income/(expense) from financial instruments designated at fair value	**496**	**113**	**(23)**		**(304)**		**282**
Gains less losses from financial investments	**29**		**460**	**(7)**	**4**		**486**
Dividend income		**1**	**16**	**2**	**1**		**20**
Net earned insurance premiums	**3,800**	**278**			**(11)**		**4,067**
Other operating income	**165**	**163**	**839**	**7**	**754**	**189**	**2,117**

Total operating income/(expense)	**12,034**	**4,921**	**8,760**	**1,962**	**(410)**	**189**	**27,456**
Net insurance claims[57]	**(4,364)**	**(342)**					**(4,706)**
Net operating income/(expense)[46]	**7,670**	**4,579**	**8,760**	**1,962**	**(410)**	**189**	**22,750**
Loan impairment (charges)/recoveries and other credit risk provisions	**(1,217)**	**(997)**	**(783)**	**(26)**	**3**		**(3,020)**
Net operating income/(expense)	**6,453**	**3,582**	**7,977**	**1,936**	**(407)**	**189**	**19,730**
Total operating expenses	**(5,166)**	**(2,378)**	**(5,265)**	**(1,296)**	**(1,151)**	**(189)**	**(15,445)**
Operating profit/(loss)	**1,287**	**1,204**	**2,712**	**640**	**(1,558)**		**4,285**
Share of profit in associates and joint ventures	**2**	**1**	**14**				**17**
Profit/(loss) before tax	**1,289**	**1,205**	**2,726**	**640**	**(1,558)**		**4,302**
	%	%	%	%	%		%
Share of HSBC s profit before tax	**6.8**	**6.3**	**14.3**	**3.4**	**(8.2)**		**22.6**
Cost efficiency ratio	**67.4**	**51.9**	**60.1**	**66.1**	**(280.7)**		**67.9**
Balance sheet data[45]							
	US$m	**US$m**	**US$m**	**US$m**	**US$m**		**US$m**
Loans and advances to customers (net)	**145,063**	**91,744**	**170,375**	**27,629**	**988**		**435,799**
Total assets	**202,431**	**111,356**	**965,462**	**76,631**	**65,824**	**(172,177)**	**1,249,527**
Customer accounts	**168,979**	**96,597**	**169,873**	**56,114**			**491,563**

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Europe	2009						
	Personal Financial Services US$m	Commercial Banking US$m	Global Banking & Markets US$m	Global Private Banking US$m	Other US$m	Inter-segment elimination[56] US$m	Total US$m
Profit/(loss) before tax							
Net interest income/(expense)	5,413	2,739	4,367	949	(525)	(675)	12,268
Net fee income	1,949	1,679	1,670	883	86		6,267
Trading income excluding net interest income	34	3	2,267	175	382		2,861
Net interest income/(expense) on trading activities	(1)	17	1,869	23	15	675	2,598
Net trading income[49]	33	20	4,136	198	397	675	5,459
Changes in fair value of long-term debt issued and related derivatives					(2,746)		(2,746)
Net income/(expense) from other financial instruments designated at fair value	1,012	133	375		(199)		1,321
Net income/(expense) from financial instruments designated at fair value	1,012	133	375		(2,945)		(1,425)
Gains less losses from financial investments	20	2	25	5	(2)		50
Dividend income	2	1	26	3	(3)		29
Net earned insurance premiums	3,975	253	(2)		(3)		4,223
Other operating income	182	373	670	28	914	95	2,262
Total operating income/(expense)	12,586	5,200	11,267	2,066	(2,081)	95	29,133

Net insurance claims[57]	(5,221)	(365)			(3)		(5,589)
Net operating income/(expense)[46]	7,365	4,835	11,267	2,066	(2,084)	95	23,544
Loan impairment charges and other credit risk provisions	(1,992)	(1,267)	(2,277)	(29)	(3)		(5,568)
Net operating income/(expense)	5,373	3,568	8,990	2,037	(2,087)	95	17,976
Total operating expenses	(5,062)	(2,294)	(4,447)	(1,183)	(907)	(95)	(13,988)
Operating profit/(loss)	311	1,274	4,543	854	(2,994)		3,988
Share of profit in associates and joint ventures	1	18	2				21
Profit/(loss) before tax	312	1,292	4,545	854	(2,994)		4,009
	%	%	%	%	%		%
Share of HSBC s profit before tax	4.4	18.3	64.2	12.1	(42.3)		56.7
Cost efficiency ratio	68.7	47.4	39.5	57.3	(43.5)		59.4

Balance sheet data[45]

	US$m	US$m	US$m	US$m	US$m		US$m
Loans and advances to customers (net)	147,760	89,084	176,123	25,541	973		439,481
Total assets	208,669	111,874	981,831	76,871	84,010	(194,655)	1,268,600
Customer accounts	165,161	102,249	169,390	58,213	6		495,019

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Europe	2008						
	Personal Financial Services US$m	Commercial Banking US$m	Global Banking & Markets US$m	Global Private Banking US$m	Other US$m	Inter-segment elimination[56] US$m	Total US$m
Profit/(loss) before tax							
Net interest income/(expense)	6,464	3,435	3,488	1,046	(459)	(4,278)	9,696
Net fee income	2,612	2,025	1,763	1,020			