HSBC

Transcript

Interim Results Announcement
H1 2023

1 August 2023, 7.30am BST

RICHARD O'CONNOR, GLOBAL HEAD OF INVESTOR RELATIONS: Good afternoon to those joining us in Hong Kong and good morning to those in London and elsewhere. Noel and Georges will present on strategy and the results and we will allow plenty of time for questions from the telephone lines and the live audience here in Hong Kong. With that, over to Noel, who'll host the conference.

NOEL QUINN, GROUP CHIEF EXECUTIVE: Thank you, Richard, and good afternoon to everyone here in the room in Hong Kong. Thank you for joining us and great to see you again. And good morning to everyone watching from London and elsewhere. Before Georges takes you through the second-quarter numbers, I'll start with a summary of the first-half performance and progress.

First, I show this slide every quarter. It's critical, in that it summarises our strategy, and our strategy remains unchanged. It is summarised by the four pillars at the bottom of the slide. Let me take you through the latest outcomes of that strategy. We had a good first six months. I'm pleased with the broad-based profit and revenue generated by our global businesses and geographies. I'm also pleased by our strong capital generation and returns.

We delivered an annualised return on tangible equity of 22.4% including the two material notable items reported in the first quarter, or 18.5% if you exclude those notable items, and we've announced a second interim dividend of 10 cents per share and a second share buy-back of up to $2 billion. Today, we're also upgrading our guidance. Now we expect to achieve a return on tangible equity in the mid-teens for 2023 and 2024.

Prior to 2023 we were very focused on transforming the business. Now, while still continuing to improve operational efficiency, we are very focused on driving growth, diversifying revenue and creating incremental value. We have a plan built around six areas. I will take you through some of these over the next few slides, starting with our international connectivity.

We grew wholesale cross-border client business in the first half by around 50%, with growth across all regions driven by higher rates. Our international proposition in Wealth and Personal Banking continues to gain traction. We now have 6.3 million international WPB customers, and that is up 500,000 or 8% over the last 12 months. That's significant because these international customers generate around two and a half times the average customer revenue. Finally, we drove strong revenue growth in transaction banking, which was up 63%.

There were good performances in Foreign Exchange and in Global Payments Solutions. Trade was slightly down year on year in line with global trade volumes, but trade balances stabilised in the second quarter, particularly in Asia, and HSBC was named best bank for trade finance by *Euromoney* for the second year in a row as well as best bank in Asia.

The next slide sets out our latest progress on another area of focus, the redeployment of capital from less strategic or low-connectivity businesses into higher-growth international opportunities. I'm pleased that we agreed new terms for the sale of our French retail banking operations in the quarter. The deal is subject to regulatory approval, and we now have a lot of work to do to complete migration in early 2024. The sale of our banking operations in Canada remains on track to complete in early 2024, with a special dividend of 21 cents per share planned thereafter. We completed the disposal of our Greek business last weekend and we have announced the disposal of our Russian operations. We are changing the nature of our business in Oman, and we will wind down our WPB operations in New Zealand.

Crucially, this is allowing us to target growth opportunities, some of which are set out on the right-hand side. The first is the continued development of our wealth business across the whole of Asia. Our digitally enabled wealth and insurance business in mainland China now has 1,400 wealth planners and is driving good new business growth. We launched Global Private Banking in India last month.

In June, we launched HSBC Innovation Banking, a strengthened, globally connected proposition on the back of our purchase of SVB UK. We will nurture the specialism we acquired, back it with HSBC's balance sheet strength and global network, and build further innovation banking businesses in the US, here in Hong Kong and Israel. The process is already well under way and will enable us to support our clients in the technology and life sciences sectors to achieve their global ambitions.

Finally, we've announced today that we are also increasing our shareholding in Tradeshift and have agreed to launch a jointly owned business in early 2024 to provide embedded financing solutions within their trade ecosystem. We believe this will help us to grow our client base in Commercial Banking, giving us a new avenue for growth outside of traditional relationship banking.

The next slide looks at how we are diversifying revenue by growing fee income and collaboration. As I've said, our wealth strategy continues to gather momentum, especially in Asia. Net new invested assets were down in the rest of the world due to lower third-party asset management liquidity products, mainly in the US, but they were up in Asia by 21% to $27 billion. Over the last 12 months, we took in a total of $75 billion of net new invested assets and grew our invested assets by 8% globally. This all underlines the growth potential of our wealth business. Fee income in Commercial Banking was up 6% in the first half and collaboration revenues between our global businesses were up 5%. Collaboration revenue is particularly important in a relatively low-growth economic environment because we can drive growth from within the organisation.

The next slide focuses on the tight cost discipline we've maintained and how it enables us to invest in the bank of the future. We remain committed to disciplined cost management and have continued to use cost savings to increase investment in digitisation. We increased spending on technology by 12.8% in the first half, and this spending now accounts for 23% of our target base operating expenses. This investment has translated into faster services, reduced friction and more competitive products, all of which will improve the customer experience and our operational efficiency.

We've made good progress increasing digital penetration amongst personal and business customers while increasing our product release frequency. Investing in technology is also enhancing our capabilities. We now have a range of test-and-learn use cases for generative AI across HSBC and are in the process of scaling up a small number of those. Last month we became the first bank to join BT and Toshiba's quantum-secured metro network. This uses quantum technology for secure transmission of data, which should mitigate the risk of future cyber-threats, and we are pleased to be working with the Hong Kong Monetary Authority on two pilots to test the Hong Kong dollar in a new payments ecosystem and to trial tokenised deposits.

My last slide shows how we have continued to build on our position as an enabler of the net zero transition. In the first half, we provided and facilitated $45 billion of sustainable finance and investments, as we continued to work closely with our clients on their transition plans. This consisted of capital markets financing and on balance sheet lending to clients and included a number of key deals in Asia and the Middle East. We were recently named Best Bank for Sustainable Finance in Asia by *Euromoney* for the sixth consecutive year.

I'll now hand over to Georges to take you through the Q2 numbers.

GEORGES ELHEDERY, GROUP CHIEF FINANCIAL OFFICER: Thank you, Noel, and a warm welcome to everyone in the room with us today. It is great to be back in Hong Kong to deliver our interim results. And for those of you watching today from London and across the globe, a very good morning and thank you for joining us.

We've announced a good set of second quarter results. Reported profits before tax were at $8.8 billion, up 89% on last year's second quarter. Revenue was up 38% at $16.7 billion. This was driven by, first, NII of $9.3 billion, which was up $2.5 billion or 38% year on year, and, second, non-NII of $7.4 billion, which was up $2.1 billion or 39% year on year.

We booked expected credit losses of $0.9 billion in the quarter. Despite the inflationary environment, cost growth in the quarter was restricted to 1% compared to last year's second quarter, including $0.2 billion of severance costs. These severance costs were expected, and we're on track to meet our 2023 cost target to limit cost growth to around 3% on our target cost basis.

Compared to the first quarter, lending and deposits were both down 1% due to subdued loan demand, deposit outflows in Global Banking and Markets in Europe and the reclassification of our portfolio in Oman to held-for-sale.

Our CET1 ratio remains strong at 14.7%. As Noel said, we announced a second interim dividend of 10 cents per share and a second share buy-back of up to $2 billion, which we intend to complete in around three months. TNAV per share was down 24 cents, due primarily to the final interim dividend for 2022 and the first interim dividend for 2023.

The next slide shows another strong quarterly revenue performance with overall growth of 38% compared to the second quarter of 2022. Three further points on this: as Noel mentioned, revenue was up in all three global businesses; wealth was up 19% due to higher rates and a strong insurance performance mainly here in Hong Kong; and, three, across Commercial Banking and Global Banking and Markets, Global Payments Solutions reported revenues of around $4.2 billion, an increase of 115% on the second quarter of 2022.

On the next slide, reported net interest income was $9.3 billion, up $0.3 billion or 4% on the first quarter. We've introduced Banking NII as a new disclosure this quarter. It is derived by adjusting reported NII for the centrally allocated cost of funding trading activities and the NII generated by the insurance business. At $11.6 billion, banking NII was up $1.3 billion on the first quarter and up $4.5 billion on last year's second quarter. The $2.4 billion centrally allocated cost of funding trading activities within Global Banking and Markets in the second quarter included a $0.4 billion year-to-date impact of methodology changes. As a reminder, the related income associated with these funding costs is reported within non-NII.

The net interest margin was 172 basis points, up three basis points on the first quarter of 2023 and up 43 basis points of the second quarter of 2022. We continue our structural hedging activity. Our NII sensitivity is $2.6 billion for a 100 basis point drop in rates against a previous year-end sensitivity of $4 billion. At this point, we are adjusting our NII guidance. We now expect NII of at least $35 billion in 2023. Within this, we expect the centrally allocated cost of funding trading activities within Global Banking and Markets to be in excess of $7 billion with associated income reported in non-NII.

We continue to reiterate that we expect to see higher pass-through rates and continued migration to time deposits, and we remain cautious on loan growth over the next six to 12 months, but we do expect it to start picking up some time in 2024. I know that many of you will have questions about Banking NII in particular, which I'll be very happy to address as we move into Q&A later.

Moving on, non-NII of $7.4 billion was down on the first quarter, which benefited from $3.7 billion of notable items and FX translation. However, it was up $2.1 billion or 39% on the second quarter of 2022. A couple of things to mention here: one, there was a strong wealth performance, up $0.3 billion or 19% on the second quarter of last year, $0.2 billion of which came from increased life insurance income primarily in Hong Kong; and, two, Markets and Securities Services was down due to lower client activity and the methodology change that I just mentioned earlier. Fees were up $0.1 billion on the second quarter of 2022 due to higher Personal Banking and Commercial Banking fees.

Turning now to credit, our second quarter ECL charge was $0.9 billion, which was $0.5 billion up on the second quarter of last year. It includes $0.3 billion for our mainland China commercial real estate exposure booked in Hong Kong and a $0.3 billion charge for the UK. To remind you, this is a more normalised level of charge that we expect for this year and is a sign that our main credit indicators are holding up.

On the basis of what we have seen so far in 2023 and ongoing macroeconomic headwinds, we continue to expect a 2023 ECL charge of around 40 basis points on average gross customer lending, including held-for-sale balances.

The next slide is our six-monthly update on our mainland China commercial real estate portfolio. As before, our principal area of focus remains the portfolio booked in Hong Kong. At the full year, our exposure was $9.4 billion. It now stands at $8.1 billion due primarily to repayments. The proportion of sub-standard and credit-impaired exposures is around 65% of the portfolio, marginally up from the full year. Of the $5.2 billion of exposures that we rated as sub-standard or credit-impaired, $1.1 billion is secured with minimal ECL due to the security held. Against the remaining $4.1 billion, we have increased our provisions from $1.7 billion at the full year to $1.9 billion today. Within this, our coverage ratio against the unsecured credit impaired exposures has increased from around 55% to nearly 70%.

At the end of 2022, we calculated a plausible downside scenario of $1 billion on this portfolio. As you can see, we have now crystallised some of that downside into the P&L. We remain comfortable with our coverage level.

On slide 17, despite the inflationary environment, cost growth was restricted to 1% on a constant currency basis versus the second quarter last year. As you can see, a large share of this growth was technology-related. There was also a higher performance-related pay accrual and the expected severance costs, which were part offset by a write-back of software and lease impairments.

We remain committed to limiting cost growth to around 3% in 2023 on our cost target basis. On this target basis, second-quarter costs were up 6% year on year, of which around half was the $0.2 billion of expected severance costs.

As a reminder, our cost target basis excludes notable items from constant currency operating expenses. It also excludes the impact of re-translating hyperinflationary economies at constant currency and, finally, it excludes the acquired cost base and additional investments in HSBC Innovation Banking, which are expected to result in incremental growth of around 1% above our targeted basis. The full cost target basis reconciliation will be on slide 26 of this deck.

Our CET1 ratio was 14.7%, which was stable on the previous quarter. Profit generation was offset by the dividend accrual of $6.9 billion during the first half and the share buy-back of $2 billion that has now completed.

In summary, this was another good quarter. There were good profit and net interest income performances. Credit remains resilient. We are on track to limit cost growth in 2023 to 3% on our cost target basis. We now expect NII of at least $35 billion in 2023 and, as Noel said, we now expect a mid-teens return on tangible equity in 2023 and in 2024, excluding the upcoming sale of Canada.

Finally, we are returning capital to shareholders by way of increased dividends and share buy-backs, and with that I'll ask the chair to open it up for questions, Richard, please. Thank you.

MANUS COSTELLO, AUTONOMOUS: Hi, thanks very much for taking my question. I wanted to ask about NII, please – a couple of questions. Firstly, I noted that the NIM was flat in Asia, in HBAP, quarter on quarter. Could you give us a bit more colour around that and what you would expect in Q3? I appreciate the trading book costs have been somewhat allocated there, but I would still have thought that you might see some benefit from higher HIBOR in HBAP. So please elucidate that performance a little bit more.

And then, secondly, you also talked about increasing hedging and the structural hedge in order to reduce your downside risk on NII. Can you go into a bit more detail about what you've done and how we should think about that in terms of potential benefits going forward into 2024 and beyond? Thank you very much.

GEORGES ELHEDERY: Thanks, Manus. So on NIM/NII, NIM in Asia was flat because most of the uplift from rates has translated into an uplift into the non-NII component of the trading book funding, about $0.3 billion uplift in that space. We've introduced Banking NII. In due course, we will enhance our disclosure in this space to introduce Banking NII sensitivity and Banking NIM, which would be reflecting such an uplift.

With regards your second question, Manus, the hedging activity – so if you look at our NII sensitivity, downwards 100 basis points, it has reduced from $4 billion to $2.6 billion. About a third of that reduction is due to our structural hedging activity and another third of that reduction will be a fact of the change of composition of our balance sheet, and then the last third is numerous other factors including modelling enhancements. If you now look at our structural hedging activity, which we've conducted over the last 12 months, the overall impact on the reduction of banking NII sensitivity is to the tune of $1 billion.

NOEL QUINN: Thank you, Georges, do you just want to explain why there's been more of a move into the non-NII trading book, what the underlying cause of that is?

GEORGES ELHEDERY: Sure, so, due to the somewhat subdued loan growth in Asia, the management of Asia has taken the decision to allocate more funding towards supporting some of the trading activities. So overall funding of our trading books globally, which was heavily used also in Asia, moved from about $108 billion or circa 6% of our deposit base to around $130 billion or about 8% or 9% of our deposit base. That additional lending or that additional transition from funds has moved NII into non-NII income. It is still rates-sensitive and it does benefit from the improved level of rates, particularly in dollars, where it's coming from.

AMAN RAKKAR, BARCLAYS: Good morning, Noel, good morning, Georges; good morning, Richard. I had two questions, please. So, again, on net interest income, at face value your 'greater than $35 billion' NII guide does imply a step-off in the run rate of net interest income in Q3 and Q4. I suspect you'd point us to the 'greater than $35 billion', suggesting that there's some conservatism that's baked in there, but can you talk to what the pressures are or indeed actually even the sources of support on the net interest income run rate from here through to year-end?

I think one thing the market would love is some sense of whether this level of net interest income is sustainable beyond this year, so anything you can give us there. I know, relatedly, that the UK has been very strong as well, so any kind of colour you can give us on the moving parts there and the sustainability of net interest income in the UK would be great.

The second question was around distributions, specifically around your dividend. You're reiterating your 50% payout ratio guidance this year. This year and potentially next year does look like it's going to be quite strong earnings. I guess if I take consensus, looking for an underlying EPS of around 120 cents, which implies an ordinary dividend of 60 cents, that number feels big. It's big versus the 51 cents you used to do; it's big versus what you did last year.

And I guess the question is how comfortable are you with paying a big ordinary dividend now which might then become quite difficult to sustain in the future, as rates come off and earnings taper? Are you bothered that you do 60 cents this year and you do some number that's lower than that next year or thereafter? Thank you very much.

NOEL QUINN: Georges, do you want to take the NII one first and clarify our position on that? Then we'll come to distributions.

GEORGES ELHEDERY: Sure. Thank you, Aman. In turn addressing your points, first, as you did say, we're emphasising this as a floor. We're emphasising this as a guidance of greater than $35 billion. We're revising this floor because we're gaining more comfort halfway into the year and with the outcomes of H1. We want to remain cautious, and you may find our guidance to be cautious given the difficulty to forecast some of the challenges I'll talk about in a second.

And then in terms of outlook for the rest of the year, look, we are not looking to change the consensus for H2 NII. We're comfortable where H2 NII stands at this stage.

Now, in terms of the pressure and the support we're seeing, we're seeing certainly tailwinds that we've seen already in Q2, one in terms of additional rate hikes, to be expected very much in the major currencies such as dollars, pounds and euros. We've seen also tailwinds in the HIBOR normalisation. We've seen about 1% quarter on quarter normalisation of HIBOR and, if you look at July, we continue seeing further normalisation. HIBOR is now around 5%, so probably around the end of July will have fully normalised, and those will provide us certainly some tailwinds as we look into H2.

This being said, we continue to see the same headwinds we've been calling out from the year-end, and they will continue manifesting in H2. The first headwind which we forecast to remain is the subdued balance sheet growth, certainly subdued loan growth due to the activity. We have indicated that we may see some resumption in 2024, but for the next half year it will probably remain as a headwind and, naturally, the other headwind that is very difficult to forecast is the deposit costs, the behaviour, what pass-through rates we will be feeding in, what is the impact of lagged migration to time deposits. In Hong Kong, we're still assuming a 1% migration per month, and whether this manifests as it is, it's very difficult to forecast, hence our cautiousness.

Now, if I look forward, look, we're not guiding for NII in 2024, but there are a few things I can just give you to bake into your analysis. The first one is you have to exclude Canada and France retail on completion of these transactions, which now we expect for Canada in Q1 2024 and in France, as we initially ambitioned, we're aiming 1 January 2024. The second one – you have to expect that balance sheet growth will resume at some stage in 2024 and that will give us support for NII. The third one is obviously the structured hedging, which I mentioned a bit earlier, and the impact they will have on more stabilisation of outlook for NII. And obviously the fourth one is what interest rate assumptions you are going to use and what pass-through rates you are going to use. And then, last but not least, we're investing a lot in our non-NII or fee income-earning businesses and do expect fee income-earning businesses to continue driving some of that growth. That's it for the NII component.

So dividends – so what we shared is that we're going to pay a 50% dividend payout ratio, excluding notable items. I think in your math, based on consensus, you have taken out notable items. I'm not going to comment on the size of the dividend, but what I'm going to say is, in order for us to sustain dividend, there are a few things we're working on, and you can as well do the math, Aman. The first one is share buybacks. As you know, share buybacks is reducing our share count, and to the extent we ambition to continue on a journey of share buybacks as long as we remain capital-generative, which is what we forecast, you have to adjust your denominator by the share count.

The second thing is the NII stabilisation actions we are taking, which should give us some protection from a reversal of the rate cycle, and the third one is obviously our cost discipline will be maintained even though we haven't yet – we are not ready to share numbers – we will maintain the discipline, and lastly, as I again indicated, fee income growth and the investments we are putting in fee-generating areas such as investment and wealth are also initiatives to support, mitigate, turn in our earnings and therefore turn and possible in our dividends beyond 2024.

RAUL SINHA, JP MORGAN: Good morning and thank you for answering my question. If I can ask two, please. The first one just on distribution is perhaps to invite Georges' thoughts on potential for buybacks in the second half of the year. Looking at your capital ratio, obviously, you probably have to make a couple of adjustments – France impact of 25 basis points, you've got the buyback that you've announced today – that's 50 basis points off the current level. Just thinking about your RoTE guidance, it does imply a slightly less capital-generative second half. Just wondering if you can scope for us, Georges, what potential buyback might be from here.

And then the second one just for Noel on wealth management revenue growth. If I look at the wealth management revenue this quarter, roughly $2 billion, just sort of stable, on Q1. I'm wondering if I understood some of the momentum that you are building within the business, so if you could just help us understand how we expect the wealth management revenue will grow?

GEORGES ELHEDERY: In terms of the buyback, obviously the fact that today we announced a $2 billion buyback will today have an impact on our Q3 CET1 ratio of 25 basis points, but you do expect us to continue generating profitability, which will build capital, 50% of which will be provisioned for dividend, as in based on a 50% dividend payout ratio anticipation, and therefore that buyback will take into the additional capital generation, so I wouldn't look at Q3 25 basis points as due to the buyback we just announced as a challenge. This is obviously just upfronting, if you want, the profit generation that we will be doing in the quarter.

Beyond that, again, at this stage what I can say is we believe we remain capital-generative for the foreseeable future, and as long as we're capital-generative, we continue to ambition a rolling series of share buybacks, but obviously we will review this on a quarter-by-quarter basis based on a number of factors, including our capital adequacy ratio.

I just want to also highlight – and probably answering your question, Raul, and complementing the question of Aman earlier – that the Canada sale expected in Q1 2024 will provide us additional capital. The priority use of the first part of it is for a 21 cents dividend, which we will be in a position to distribute expected in H1 2024, and then the residual part of it we will utilise to supplement or complement or top up any capital buyback we are planning to do.

NOEL QUINN: Thank you, and I think it's a fair comment on your second question that what we are talking about here is very much growth in lead indicators. The $27 billion of net new invested assets here in Asia in the first half, up 21%. Globally, net new invested assets growth of $75 billion over the past 12 months, a growth in our aggregate invested assets of 7% globally. They are strong lead indicators – an additional half a million international customers in the past 12 months. For me, they are the lead indicators.

I think you're absolutely right. There will be a lag effect as you turn that customer acquisition and asset acquisition into revenue, but that's why we're talking about building businesses and new growth opportunities that can supplement our revenue going forward and give us some cushion and offset to any downside rate effect that may emerge post-2023 and post-2024, so we think it's the right thing to do, and you're right – the revenue will be a lag indicator on those early success criteria that we're sharing with you.

If you remember our growth in our wealth business in mainland China, we started with zero wealth managers just over two years ago. We've now got 1,400. Our ambition is to get to 3,000 over the relatively near term over the next couple of years or so. Again, that will be revenue generative as an offset because most of that is fee-based as an offset to any downside pressure that may be on interest rates, so I think your second comment is a fair comment, but I'd turn that into the positive rather than the negative.

RICHARD O'CONNOR: And Raul, just to add, as you're aware – Q1 is normally seasonally a bit stronger and IFRS 17 means you build revenue from a pretty low base but up rapidly.

ANDREW COOMBS, CITI: Good afternoon. Two questions, please. Firstly on Chinese commercial real estate, there were ups in the charges in Q1, and more additional charges in Q2, what triggered those additional charges? And then when you talk about your downside scenario on slide 16, I think previously you'd said $1 billion; you're now saying lower. Should you just take off the $0.3 billion and say $0.7 billion, or can you provide some framework around what you think the downside scenario now is?

And then my second question – perhaps I could just invite you to make some comments on the FCA's 14-point plan on cash savings that was released yesterday and any implications you think that might have for the UK business? Thank you.

GEORGES ELHEDERY: Thank you, Andrew. So we have put in more charges in Q2. The total charges was $0.3 billion – or the sum of Q1 and Q2, Q1 being very benign, is $0.3 billion. Most of these charges are on stage 3s. These are more technical adjustments over names that have defaulted. So where we stand now in terms of charges is we are comfortable with the charges we have against this portfolio on China CRE. Now, with regards the plausible downside scenario, we indicated $1 billion at the year-end as a plausible downside. We have indeed crystallised $0.3 billion of it, so without being precise on the math here, it is indeed a residual circa $0.7 billion that remains a plausible downside, which may or may not materialise over the coming few quarters.

NOEL QUINN: Thank you, and with regard to the FCA and the work they're doing on savings accounts – I think was your second question – listen, we believe in both the mortgage book and the savings – the deposits book – we have tried to make sure that we are offering a good range of products to our clients whereby they have choices. So on savings, we've got a good, competitive range of fixed-rate deposit accounts in the market. We also believe we've got good pricing in place for more instant access type savings accounts or deposit accounts. We will participate with the FCA on any review they do. We believe if you take our two-year fixed-rate savings account in the UK, based on the yield curve in the UK, we're offering savers the opportunity to get 5.1% on that two-year fixed-term savings account. If you compare that to our two-year fixed-mortgage product that we're offering to our customers with a 60% loan-to-value ratio, we're in the market at around about 5.53%, and for new-to-bank customers we'd be in the market at about 6.1%.

So we believe we have the structure of the deposit book and the structure of the mortgage book in the right level, and as ever, there is a price difference between term product and instant access product because of the maturity and the liquidity risk, so we have tried to price our products fairly and appropriately. We're very cognisant of the pressures that UK customers face at this point in time. We've certainly tried to remain competitive and to help them navigate what is going to be a challenging year or so, with high interest rates in the yield curve and higher rates of inflation, but we will fully participate with any review that the FCA take. We're also trying to encourage, through marketing prompts, customers to take advantage of those products if they want them and they meet their circumstances. We can't and should not force them into term savings, but we need to make sure they're aware of our term savings products should they want to take advantage of it.

KATHERINE LEI, JP MORGAN: Hi, I have two questions. One is more long term and one is more near term. For the long-term questions, I will ask management if you can give us any colour on potential impact of Basel III reform, because I think one of the key support on share prices is buyback and shareholder return, and then I think the impact of capital because of these potential regulatory changes will have an impact on how we model in future capital return, but this is more in the long-term. I understand that. I just want to get some colour – any colour – particularly after the US regulator released that Basel III endgame. How would that change our present forecast on that? So this is for the long-term question.

And then on the near term, just now I think management gave us a number – a potential additional ECL charges on China CRE $0.7 billion, and then I also noticed that for our guidance for full-year credit cost is 40 basis points, but if I look at the first half, it's a bit less than 30 basis points on an annualised basis, so that additional upside on credit costs – have we included that $0.7 billion or that $0.7 billion is outside of the 40 basis points guidance?

NOEL QUINN: I think I'll take the second one first and then ask Georges to cover the more technical, difficult Basel III question. So on the ECL, we decided to maintain guidance at 40 basis points on ECL because there is still a lot of economic uncertainty out there. There's economic uncertainty around China's commercial real estate. There's economic uncertainty generally in the world. We've had a good first half performance on ECL, as you say. $1.3 billion is below the run rate of 40 basis points, so we think we do have some capacity to absorb some of that risk that's inherent in the commercial real estate book in China, but I think I'd be misleading you if everything was so scientifically proven, because it all depends on what happens elsewhere in the world.

So, I could easily say, 'Yes, we've got capacity to absorb that,' but it depends what happens elsewhere in the world, but we do believe we have – it's right to maintain a conservative guidance at the moment on ECLs at 40 basis points, and we have capacity in the second half, relative to the first half performance, to absorb some additional shocks, should they come through from near-term economic issues. Georges, do you want to handle Basel III?

GEORGES ELHEDERY: Yes, maybe just finishing on the ECL point, I would caution you not to annualise H1. If you look at Q2 at $0.9 billion as a more normalised level, so that is more a level that you can look at, whereas Q1 was unusually quite low, so this is why H1 will look low to your taste.

So on Basel III, the first thing to share about Basel III is we need to know the final rules. At this stage, most of these rules are still in draft form, and they will remain subject to change as we know the final rule.

The second thing I will share is that, based on the current draft rules as per our PRA standards for the Group holdings, there will be a minor improvement initially in our RWAs, but as the output floor starts kicking in five years into the journey, so from 2025 plus five years, there is a likelihood that the outputs floor will catch us and that the impact may be in a material up or down – but immaterial up as we look at it this way.

This being said, I just want to caution one thing. The US obviously issued their draft rules last week. They came out more severe than we initially expected. They will have an impact on our US operations. It remains a marginal impact. We're likely talking single-digit RWA uplift against a possible downward move before that, but those rules will impact our local reporting for our US entity – will not change the way we report at the group level, so we will need to navigate both, if you want, in parallel.

NICK LORD, MORGAN STANLEY: Again, a couple of questions if I may, please. I think Georges has given a very thorough description of how you might sustain earnings post return end rates, but obviously a lot of that fee generation is going to come at a cost, so I just wonder if I could invite you to talk about how you think of balancing that fee generation with cost in the next two to three years.

And then secondly, a little bit more specific, but you're now three or four months into having bought SVB. We've spoken a little bit about it here. I just wonder if you could give us a little bit more detail on how your plans have evolved for that business.

NOEL QUINN: Yeah, thanks Nick, and by cost I'm assuming you mean investment cost to get to it.

NICK LORD: It's how you manage investment costs against operating costs, yes.

NOEL QUINN: Yes, that's fair. Listen, you're absolutely right. We're keeping a strong and tight cost discipline in the bank, but what we're doing is we're reallocating cost "from / to", and what we're typically reallocating is from what I'd call bad costs – costs that are associated with low returning portfolios, low returning business activities in certain markets or costs that are associated with manual processes that should be digitised – so if you look at our cost performance, I think we increased our investment in IT costs by 12% so far this year – first half to first half – we increased some of our investment cost in our global businesses, and we reduced cost elsewhere, and that's what's getting us back to the 3%.

So we're investing and saving at the same time, and that is a phenomenon that probably, historically, HSBC has not been great at. It has typically been cost management or cost investment, and it has been a cycle. You manage costs tightly, and then you invest. We're definitely trying to do both at the same time, and there's a lot of self-funding going on to try and mitigate the overall cost base, and that's how we're building out the 1,400 people in mainland China, because we're saving cost through other country exits, other market exits, reducing our support costs in some of the manual processes in our global processing centres. That's allowing that investment to take place, and that's been the journey for the past three years.

On SVB, the integration is going well. We've had no nasty surprises since the day we bought the business. It was profitable the day we bought it. It is still profitable. We're going through systems migration at the moment. One statistic which is probably an important guide for the future – in the three months post-acquisition, we took in new-to-bank customers at a higher rate than the three months prior to acquisition, so in the transition of ownership from the previous owners to us, we've seen an uptick in the momentum of customers wanting to bank with SVB in that first three-month period. That acquisition has also given us the knowledge, the platform, the connections, and frankly, the positive brand and reputation globally that has allowed us to go and recruit a team in the US. We recruited a team here in Hong Kong and we've recruited a team in Israel.

So my view that there is strong growth prospects in that business, not just for the next two or three years – I'm doing this because I think this will be an important business for us in the five to 10 to 15-year timeframe. This is an important sector of the economy and we're willing to invest in it, so I'm very pleased with how it's going. We probably do owe you, as an investment community, more detail on how material, what are the numbers, and I'll think we'll come back to you at the end of the year with, if you add this all together, the investment and the current bought business, what could that potentially look like going forward and how material is that, but that is something, if it's okay, we'll give you more towards the end of this year with the full-year results.

GUY STEBBINGS, BNP PARIBAS: Hi there, thanks for taking questions. Good morning and good afternoon all. I had one back on costs, and then one on NIM specifically in the UK. On costs, in the context of a very strong top line and then uprated RoTE guidance this year and next year, I'm just interested in how you're thinking about investment spend in that context of what is a better revenue backdrop that you had previously anticipated. Guidance is very clear for this year, but does it change your attitude at all for next year and beyond, also mindful of consensus - modest growth next year from where you're guiding in the market - so just how deliverable or appropriate you think that is in the context of what is a better top line and given the opportunity available to you?

And then the second question was on NIM in the UK. You saw a very strong growth in the second quarter in the ringfenced bank, in stark contrast to some UK peers. If you could talk about some of the dynamics, how you see the deposit mix evolving. I appreciate it's very difficult to be too specific, but if there's any perspectives there, and whether ultimately NIM in the UK ringfenced bank is likely to peak now at this level.

NOEL QUINN: Thanks. Certainly on costs it's a very simple answer. We're not giving any guidance at this stage on 2024. We'll give an update on 2024 guidance at the end of the year, but on 2023 we've given, I think, a strong commitment on cost discipline. I also will maintain strong cost discipline in 2024, but I'm not going to quantify what that means in terms of percentage growth at this stage. On the UK, Georges, it would be good if you could just share some of the information that we've got on the UK, particularly the progress we're still making in the UK mortgage market, despite the pressures in the UK mortgage market. It would be good to put some colour on that, please.

GEORGES ELHEDERY: So Guy, maybe I'll start by talking about the dynamic and I'll delve into NIM specifically, but first, in terms of passthrough rates on the deposits, for the last 50 basis points of rate hikes from the Bank of England, we've passed through to our retail savings rate around 70% so we believe, from a consumer point of view, we are competitive having passed through, and obviously this is a higher than 50% passthrough. The overall book passthrough is in the around between 40% and 50%, but clearly the marginal passthroughs are higher at these high level of rates. Equally on the mortgages, we continue aiming for market share, so we've grown the stock market share from 7.7% to 7.8% and our new business market share is now just shy of 10%, so we maintain a leading proposition in mortgages.

Now if I go specifically on the NIM, without talking to our peers, some parameters that you can use when you're doing your assessment and your analysis – the first one is we have a very strong liquidity position with a very strong deposit franchise and a low loan-to-deposit ratio. The second one to take into account is we are relatively small in consumer finance, so that component of our portfolio is single-digit percentage of our retail finance. The third one to take into account is that our structural hedging is relatively young, i.e. we started the structural hedging essentially when rates started to be at higher levels, so we have little baggage from structural hedging positions from prior, i.e. when rates were very low, and this is obviously helping us in adjusting our NIM upwards, and we're not bugged by low-interest-earning assets from older structural hedges. And in terms of expectations, I think it's fair to expect that the increase we've seen in Q1 is unlikely to be repeated as we look into the rest of the year.

TOM RAYNER, NUMIS: Good morning. Just on your revised RoTE guidance 2023 and 2024, it's in the mid-teens, excluding the material notable items. I understand when I look at your company consensus, you have got material notable items in there. I think the sale of Canada is boosting the consensus return, so my point and my question is I think that that potentially obscures the size of the underlying upgrade that you're guiding to for return on tangible equity in 2024, and my concern is whether the way you now present the figures, because the notables now are part of your numbers and therefore I think it makes sense for the consensus to look at it that way, but I'm just wondering whether this presentation is making it more difficult for investors to understand the underlying drivers of the business and whether that is maybe even affecting your rating at some level. I just wondered if you could comment on that.

GEORGES ELHEDERY: Our RoTE guidance of mid-teens initially has been excluding notable items, so for this year, obviously we had two notable items in Q1: the provisional gain of SVB, $1.5 billion, but also the reversal of the impairment of the French retail business, $2.1 billion. As we look to year-end, we do anticipate that we will reinstate this impairment sometime in H2 for a possible, obviously, closure of the transaction on 1 January, so that notable item, if you want, washes itself out from our full-year expectations.

As regards 2024, I think the Canada impact is a couple percentage points on our RoTE, so whether you stretch the mid-teens a little bit on either side, you may still be right, but we would like to take it out because obviously it remains – while we are very confident in the resolution – it remains an element that is subject to continued regulatory approvals, so you can do your math with or without.

NOEL QUINN: So I suppose the way we are looking at mid-teens as – if you look at the first half - we printed a headline rate of 22.4% RoTE. If you take out the two notable items, you get to an 18.5% RoTE. We're guiding mid-teens to be equivalent, you could say, with the 18 number, not the 22 number, and if you think about 2024, there'll be a profit on sale of Canada, assuming that transaction completes. There will be a capital policy around that in the form of dividend and in the form of buybacks, but we're not including that profit on sale within our guidance – we're not including that in our definition of mid-teens. That's over and above.

So what we're trying to say we're giving you a mid-teens RoTE guidance for the core business, not with the big swings in M&A activity achieving it. That's the way I'd look at it, so we just want to try and make sure everyone understands what we mean by mid-teens, and it doesn't include the big one-offs – either the one-off positives or the one-off negatives. We're looking at the fundamental business in guiding to that.

GEORGES ELHEDERY: And just adding – complementing that – we're not trying to change consensus at this stage.

TOM RAYNER: Can I just quickly come back on that, because the real question – thank you. I guess my real question is this mid-teens – is this now what you view as more of a through-the-cycle type level of probability – because if you look at consensus for 2025 at the moment, it ends up dropping away again, because I guess people – the one-offs have dropped out, but it sounds to me as if you think now interest rates have normalised to a level where they're more realistic than they've been for maybe the last decade or so, and maybe your profitability mid-teens is now what you're comfortable with. Is that what you're saying on more of a through-the-cycle basis?

NOEL QUINN: I think you've overread it, because what we said is the guidance is for 2023 and 2024. We're not giving you guidance for 2025 and beyond. We will do that at some stage, so I wouldn't overread that. Clearly, in 2025 and beyond you've got interest rates that will start to come off, but I'm also talking about building alternative revenue streams, building balance sheet growth because as interest rates come off, economic recovery improves and the balance sheet will start to grow again. So our job as a management team and our philosophy is we want to try and make sure we can mitigate some of that downside risk, either through hedging or alternative growth strategies to stabilise the RoTE over time, but for the avoidance of doubt, we are not guiding at the moment on 2025 RoTE. We're only guiding on 2023 and 2024, and we'll have to see how the economics of the world develop, and I think Georges should probably reiterate what he said at the end of that, because the line went a bit hazy, Georges, on consensus.

GEORGES ELHEDERY: Look, we're not trying to change consensus – where we see consensus for our RoTE for 2023 and 2024.

PERLIE MONG, KBW: Hello, I've just got two questions. The first one is perhaps on non-interest income, especially in wealth in Asia. If I look at your Asian entity reporting and look at revenues, it's pretty flat quarter on quarter, but NII has gone up a little bit, so that suggests to me that non-interest income has come down a little. I'm just wondering what you see in the frontline, especially with regards to wealth and obviously Hong Kong's GDP print yesterday was quite a bit weaker than expected, so just what you see in context and your expectation about your Chinese business and to what extent do you think that that might help you. So that's my first question.

And then the second question is on deposit migration in Hong Kong because I noted in slide 41 it looks like Hang Seng, which is obviously traditionally very strong retail savings franchise, it looks like deposit migration went the other way, so does that suggest that migration is nearly there in Hong Kong and is it topping out?

GEORGES ELHEDERY: On the non-NII wealth in Asia, you will observe actually the biggest pick-up is in insurance – sorry, first taking the impact of funding the trading book, which is showing under non-NII and is material, it's $1.2 billion. If you take this one out, the growth is essentially from insurance and insurance in Hong Kong. It does appear under non-NII, but not fee income. That growth is a reflection of the growth we've seen in Q1. It's in the 40% to 50% growth year on year. It is reflective of the opening of the border between China and Hong Kong and the additional inflow of mainland Chinese new policies in our Hong Kong business. About 30% of new policies are from mainland Chinese. As you would expect, insurance is a core component of wealth, in particular here in Hong Kong, and that's the main driver of the growth.

We still see some softness in wealth with regards equities trading, and that's more reflective of the equity markets in general, and I want to say while the Hong Kong GDP is the main driver of our loan portfolios in terms of growth in our balance sheet, wealth activity is not necessarily directly linked to the GDP. It is linked to investor behaviours and it is linked to sentiment in the market.

With regards your second question on migration, in HSBC we continue to see a migration of around 1% per month, although it did slow a little bit in April, but that continued a trend that we have been forecasting, whereas in Hang Seng, where the term deposit share is in the mid-30s percent. Our colleagues in Hang Seng have taken a proactive approach to manage some of the highly rate-sensitive deposits, and allowed them, if you want, to accept some attrition against these highly rate-sensitive or rate-chasing deposits, and this is what allowed them to maintain or slightly reduce their term deposit mix. They're benefiting from a very strong liquidity position and a strong deposit franchise, and they do not need, necessarily, highly rate-sensitive deposits at that margin.

SAM WONG, JEFFERIES: Thank you. Congratulations on the strong results. Just a very quick question on Hong Kong mortgages. The mortgage rate in Hong Kong right now is well below HIBOR. Many smaller banks are actually backing off from the mortgage market, so do you see mortgage pricing in Hong Kong going up? What would be the implications for that? That's the first question.

The second question is on China. There are a lot of macro concerns going on right now, so how would you navigate through the macro uncertainties as a bank? Thank you.

GEORGES ELHEDERY: I can take the first part. Sam, first our mortgage – we continue printing mortgages. Yes, indeed the rates are quite attractive for borrowers. And we increased our mortgage book, not a very large amount, but we increased our mortgage book. So we continue – and this is despite subdued property sales in Hong Kong. We continue increasing our book. On the pricing, as you know, the mortgages are capped and the pricing is highly correlated to the savings rate. For instance, last week we increased the saving rate by about 12.5 basis points on the Hong Kong dollar. It automatically increases the cap, and therefore the mortgage pricing today, by 12.5 basis points. I see this as a natural evolution with rates, not a specific pricing for the mortgage or a specific dynamic for the mortgage pricing, if you want.

NOEL QUINN: In terms of China macro – so, we had a brief conversation before. If you take all of the international banks' share of the corporate debt market in mainland China, I think all of us together are about 2% market share. So actually, growing your corporate banking business as an international bank, particularly if your strategy is connecting mainland China to the rest of the world in both directions – GDP is not the prime driver of growth in the sense of what you can do, because you're still relatively niche in the market, and what is a huge market, so you can get growth despite the fact that GDP – and by the way, GDP is still 5%-plus, so it's not bad, but you can still get growth.

Similarly, in our wealth business that we're pursuing in mainland China we're pursuing an area which is around about helping internationally-orientated personal customers, and particularly the domestic customers in the Greater Bay Area get access to wealth products and insurance products to help them with their protection needs and their savings needs. That is primarily targeted at the affluent or the emerging affluent sector rather than particularly at the high net worth or ultra high net worth. That is the core business we have here in Hong Kong.

The way I look at it is that the wealth proposition here in Hong Kong has been a very strong driver of growth and profitability for HSBC in Hong Kong. Will we see that same opportunity in the Greater Bay Area? The engagement between the Greater Bay Area – or the Guangdong province – and Hong Kong represents a significant long-term growth opportunity for us, and what we're trying to do, which is different to three or four years ago, is we're targeting international wealth and insurance as our primary proposition, as opposed to just becoming another mortgage provider or another card provider in Guangdong province. We see opportunity for growth. Yes, you can't ignore the macro environment, but we do see conditions for good growth for our business in mainland China.

JOE DICKERSON, JEFFERIES: Just a quick question, and most have been asked and answered. Just on the dividend question that Aman asked, the answer was slightly longwinded. If I interpret what you're saying, it sounds like you would like the dividend – the ordinary to be progressive?

Secondly, can you just discuss from the Hong Kong business or the HBAP business the NIM trend that was flat, quarter on quarter? How much was the US dollar-denominated business in play there, because if I look at your rate sensitivity disclosures the USD bucket now looks liability-sensitive as opposed to asset-sensitive. How much of the NIM movement there, in an adverse sense, was attributed to the US dollar business, or was it something else?

NOEL QUINN: Let me deal with the dividend one first. The guidance we've given is that for 2023 and 2024 we'll have a 50% payout ratio. In addition, we've guided to the first use of proceeds of Canada's sale proceeds will be a 21 cents special dividend. We're not giving any guidance on whether the dividend's progressive or not progressive. We're only giving the guidance that we've just said, which is 50% of profits. Clearly as a management team our ambition is to make our profits progressive, but we're not guiding on dividend as a progressive dividend policy. Our policy is 50% payout ratio, and that will be a function of earnings. Georges, do you want to cover Hong Kong NIM?

GEORGES ELHEDERY: On the Hong Kong NIM, the NII increased by \$0.1 billion but the banking NIM increased by \$0.4 billion because the non-NII component of the trading funding increased by \$0.3 billion. Now, the way the statutory NIM is computed is only looking at the NII component, and therefore it's showing flat, but as I mentioned, we will be upgrading our disclosures and enhancing our disclosure with regards to the Banking NIM. That will give you move visibility on the overall margin when you take into account the funding of the trading book.

Now, in terms of sensitivity to the USD you're actually also driving towards the same dynamic in the funding of the trading book. Dollars has been a currency that we fund a number of our activities with, so when you look at the NII sensitivity dollars comes opposite to all the other currencies, because that's a funding currency. Essentially dollars is funding our funding of the trading book, and therefore when you look at the funding book sensitivity we've put in a few explanations on the slides where we estimated this to be to the tune of \$1.3 billion. It is fair to assume most of it is dollars, and therefore reverses it and renormalises our dollar sensitivity overall on the balance sheet to be that of a negative sensitivity for minus 100 basis points.

NOEL QUINN: I just want to say thank you very much for all of your questions and your time today. We really appreciate you spending some time with us.

Just to close with a couple of comments. We've had a good first six months. I'm pleased with how the business is performing. We've delivered an annualised return on tangible equity of 22.4%, or 18.5% excluding those notable items. We've increased dividends and buybacks. I'm also confident about the future. We still have opportunities to drive growth and to diversify revenue while retaining tight cost control. We have upgraded our returns guidance for 2023 and 2024. Richard and the team are available to you if you have any further questions, but in the meantime have a good rest of the day. Thank you very much.