HSBC Holdings plc

6-K specific disclosures
30 June 2019

HSBC

Risk elements in the loan portfolio

Unless otherwise stated, the disclosure of credit risk elements in this section reflects US accounting practice and classifications. The purpose of the disclosure is to present within the US disclosure framework those elements of the loan portfolios with a greater risk of loss. The three main classifications of credit risk elements presented are:

- impaired loans;
- unimpaired loans contractually more than 90 days past due as to interest or principal; and
- troubled debt restructurings not included in the above.

Impaired loans

In the following tables, we present information on our impaired loans and advances in accordance with the classification approach described in the *Annual Report and Accounts 2018.*

A loan is impaired, and an impairment allowance is recognised, when there is objective evidence of a loss event that has an effect on the cash flows of the loan which can be reliably estimated. In accordance with IFRSs, we recognise interest income on assets after they have been written down as a result of an impairment loss.

The balance of impaired loans at 30 June 2019 has remained stable at $13.3bn when compared to 31 December 2018. This is a reflection of the benign credit environment.

Unimpaired loans more than 90 days past due

Under IFRS 9 the Group determines that a financial instrument is credit-impaired and in stage 3 by considering relevant objective evidence, primarily whether:

- contractual payments of either principal or interest are past due for more than 90 days;
- there are other indications that the borrower is unlikely to pay such as that a concession has been granted to the borrower for economic or legal reasons relating to the borrower's financial condition; and
- the loan is otherwise considered to be in default.

If such unlikeliness to pay is not identified at an earlier stage, it is deemed to occur when an exposure is 90 days past due, even where regulatory rules permit default to be defined based on 180 days past due. Therefore the definitions of credit-impaired and default are aligned as far as possible so that stage 3 represents all loans which are considered defaulted or otherwise credit-impaired. Interest income is recognised by applying the effective interest rate to the amortised cost amount (i.e. gross carrying amount less ECL allowance).

As a financial instrument is considered impaired if contractual payments of either principal or interest are past due for more than 90 days, these amounts will be reported under impaired loans with no balance reported under unimpaired loans more than 90 days past due.

Troubled debt restructurings

Under US GAAP, a troubled debt restructuring ('TDR') is a loan, the terms of which have been modified for economic or legal reasons related to the borrower's financial difficulties to grant a concession to the borrower that the lender would not otherwise consider. A modification which results in a delay in payment that is considered insignificant is not regarded as a concession for the purposes of this disclosure. The SEC requires separate disclosure of any loans which meet the definition of a TDR that are not included in the previous two loan categories. Loans that have been identified as TDRs under the US guidance retain this designation until maturity or derecognition. This treatment differs from the Group's impaired loans disclosure convention under IFRSs under which a loan may return to unimpaired status after demonstrating a significant reduction in the risk of non-payment of future cash flows. As a result, reported TDRs include those loans that have returned to unimpaired status under the Group's disclosure convention for renegotiated loans.

The balance of TDRs not included as impaired loans at 30 June 2019 was $2.2bn, $0.5bn lower than at 31 December 2018. Under the Group's IFRS 9 methodology financial instruments (except for renegotiated loans) are transferred out of stage 3 when they no longer exhibit any evidence of credit impairment. Wholesale renegotiated loans will continue to be in stage 3 until there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows, observed over a minimum one-year period and there are no other indicators of impairment. For loans that are assessed for impairment on a portfolio basis, the evidence typically comprises a history of payment performance against the original or revised terms, as appropriate to the circumstances. For loans that are assessed for impairment on an individual basis, all available evidence is assessed on a case-by-case basis. Retail renegotiated loans are deemed to remain credit impaired until repayment or derecognition.

Potential problem loans

Potential problem loans are loans where information on possible credit problems among borrowers causes management to seriously doubt their ability to comply with the loan repayment terms.

Under IFRS 9, an assessment of whether credit risk has increased significantly since initial recognition is performed at each reporting period by considering the change in the risk of default occurring over the remaining life of the financial instrument. Any financial instrument deemed to have suffered a significant increase in credit risk is transferred from stage 1 to stage 2.

The assessment explicitly or implicitly compares the risk of default occurring at the reporting date with that at initial recognition, taking into account reasonable and supportable information, including information about past events, current conditions and future economic conditions. The assessment is unbiased, probability weighted and, to the extent relevant, uses forward-looking information consistent with that used in the measurement of ECL.

The analysis of credit risk is multifactor. The determination of whether a specific factor is relevant and its weight compared with other factors depends on the type of product, the characteristics of the financial instrument and the borrower, and the geographical region. Therefore, it is not possible to provide a single set of criteria that will determine what is considered to be a significant increase in credit risk and these criteria will differ for different types of lending, particularly between retail and wholesale. However, unless identified at an earlier stage, all financial assets are deemed to have suffered a significant increase in credit risk when 30 days past due. Financial instruments classified as stage 2 and greater than 30 days past due are considered to have a higher risk of containing potential problem loans.

'Renegotiated loans and forbearance' on page 58 of the *Interim Report 2019* includes disclosure about the credit quality of loans whose contractual terms have been changed at some point in the life of the loan because of significant concerns about the borrower's ability to make contractual payments when due. Renegotiated loans are classified as impaired when:

- there has been a change in contractual cash flow as a result of a concession that the lender would otherwise not consider; and
- it is probable that without the concession, the borrower would be unable to meet contractual payment obligations in full.

This presentation applies unless the concession is insignificant and there are no other indicators of impairment. The renegotiated loan will continue to be disclosed as impaired until there is sufficient evidence to demonstrate a significant reduction in the risk of non-repayment of future cash flows, and there are no other indicators of impairment.

Renegotiated loans that are not classified as impaired may have a higher risk of becoming delinquent in the future, and may therefore be potential problem loans. Further information regarding the credit quality classification of renegotiated loans can be found on page 56 of the *Interim Report 2019*.

Analysis of risk elements in the loan portfolio by geographical region

The analysis below sets out the amount of risk elements in loan portfolios included within loans and advances to customers and banks in the consolidated balance sheet, trading loans classified as in default and assets obtained by taking possession of security.

The table excludes the amount of risk elements in loan portfolios classified as 'assets held for sale' in the consolidated balance sheet.

Risk elements in the loan portfolio by geographical region

	At	
	30 Jun 2019	31 Dec 2018
	$m	$m
Impaired loans	**13,335**	13,347
– Europe	**6,517**	6,434
– Asia	**2,331**	2,521
– Middle East and North Africa	**2,275**	2,233
– North America	**1,561**	1,500
– Latin America	**651**	659
Unimpaired loans contractually more than 90 days past due as to principal or interest	**–**	–
– Europe	**–**	–
– Asia	**–**	–
– Middle East and North Africa	**–**	–
– North America	**–**	–
– Latin America	**–**	–
Troubled debt restructurings (not included in the classifications above)	**2,237**	2,725
– Europe	**1,412**	1,682
– Asia	**78**	98
– Middle East and North Africa	**493**	527
– North America	**170**	229
– Latin America	**84**	189
Trading loans classified as in default	**–**	–
– Europe	**–**	–
– Asia	**–**	–
– Middle East and North Africa	**–**	–
– North America	**–**	–
– Latin America	**–**	–
Risk elements on loans	**15,572**	16,072
– Europe	**7,929**	8,116
– Asia	**2,409**	2,619
– Middle East and North Africa	**2,768**	2,760
– North America	**1,731**	1,729
– Latin America	**735**	848
Assets held for resale	**62**	76
– Europe	**14**	16
– Asia	**28**	39
– Middle East and North Africa	**–**	–
– North America	**13**	12
– Latin America	**7**	9
Total risk elements	**15,634**	16,148
– Europe	**7,943**	8,132
– Asia	**2,437**	2,658
– Middle East and North Africa	**2,768**	2,760
– North America	**1,744**	1,741
– Latin America	**742**	857
	%	%
Loan impairment allowances as a percentage of risk elements on loans	**54.8**	53.7

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