Group Chairman's Statement

The Group delivered strong results across its major businesses, providing further evidence of a successful repositioning. Its diversified business model, international network and capital strength provide a solid foundation for further growth.

Douglas Flint Group Chairman

As the Group approaches a periodic transition in leadership, it is extremely pleasing to report that, in the first half of 2017, it delivered a strong set of results across its major businesses. As well as being financially robust, these results added further evidence of the successful repositioning of the Group since 2011. This has created a solid foundation, with attractive optionality, for the future.

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The benefits of diversification, combined with the Group's capital and funding strength, once again were apparent. Notwithstanding uncertainties arising from increasing geopolitical tensions and ambiguous predictions around the shape of transition to, and final form of, the UK's future relationship with its major trading partners in the EU, customer activity across all business segments was resilient.

Markets-based revenues benefited from market share advances, commercial banking customer activity was robust, wealth management and insurance revenues were notably stronger in Hong Kong, and credit experience globally remained remarkably sound. As central bank interest rates edged higher, led by the US, we began to benefit from improved margins on our core deposit bases, providing a welcome enhancement to the Group's revenue mix, given the likely trajectory of interest rates over the medium term.

These factors drove reported profit before tax for the Group in the first six months of 2017 to $10.2bn, 5% higher than what was achieved in the first half of 2016. Earnings per share amounted to $0.35 (1H16: $0.32).

On the adjusted basis used to assess management performance, pre-tax profits were $12.0bn, 12% higher than in the comparable period. It was particularly pleasing to note improvements within both revenue and cost performance that derive from management actions taken in recent years to reshape the Group around its core strengths. Stuart Gulliver will address these in more detail in his review.

The Group's capital position remains strong, with the common equity tier 1 ratio standing at 14.7% at 30 June (31 December: 13.6%). During the period we completed the further share buy-back of $1bn that the Board approved in February and, also as previously announced, we maintained the first two dividends in respect of the year at $0.20 in aggregate, in line with the prior year. In light of the strong capital position, the Board approved a further buy-back of up to $2.0bn of ordinary shares, planned to commence shortly after publication of these interim results.

HSBC is now better positioned for the future

Management continued to make good progress against the strategic targets laid out in June 2015. The first half of the year included a number of important events that will contribute to the strengthening of HSBC's position in our two home markets and in core product areas.

One of the most significant opportunities for HSBC going forward is participation in China's domestic capital markets as these open up. Meaningful progress in this regard was made in the first half of this year, which saw the granting of further access to undertake domestic corporate bond underwriting and the establishment of Bond Connect, which enables offshore investors to trade onshore Chinese interbank bonds through Hong Kong. In equity markets, Chinese stocks traded higher in part on MSCI's decision in June to include them in its global benchmark equity index for the first time.

Given these developments, we were delighted to receive approvals at the end of June enabling The Hongkong and Shanghai Banking Corporation to establish the first joint venture securities company majority-owned by a foreign bank. This will enable HSBC to offer a broad spectrum of securities and investment banking services nationally, and is an important step in building out our global banking and markets capabilities to serve the Chinese capital markets.

The second area to highlight is the value of our network and how we are investing to enhance that value. HSBC's position as the leading bank in trade finance reflects its unique global network and heritage. Technology is offering important opportunities to automate and digitise paper-heavy supply chain processes, and organise supply chain financing on a single platform. For example, HSBC, working with its strategic business commerce partner, Tradeshift, is now offering an integrated solution to enable our clients to manage their global supply chains and working capital requirements from a simple online platform. This will improve transparency and reduce costs.

In terms of structural change, the creation of the UK ring-fenced bank to meet the central recommendation of the Independent Commission on Banking in 2011 has been one of the largest projects ever undertaken by the Group. At its peak, the project team numbered more than 2,000 and costs to date amount to approximately half a billion dollars. In early July, the Prudential Regulation Authority approved a restricted licence for the new bank, representing an important milestone in meeting our legal obligations. We are targeting 1 July 2018 as the deadline to operationalise the UK ring-fenced bank, ahead of the statutory implementation date of 1 January 2019. Transition towards this deadline will be a key execution priority.

Finally, the Board was delighted that the successful transformation of the Group over the last six and a half years was recognised through HSBC being awarded the accolade of the 'World's Best Bank' earlier this month by *Euromoney* magazine. This award reflects the extraordinary efforts of the management team and all of our colleagues in reshaping the Group to meet the expectations of all our stakeholders. As ever, we owe them our sincere gratitude.

As I head towards retirement from HSBC later this year, I have taken the opportunity to set out the three public policy issues that are top of mind in terms of allowing the financial system to serve the global economy better.

Regulatory fragmentation must be avoided

The new administration in the US is leading the rest of the world in applying a retrospective lens to the aggregate of regulatory changes implemented and proposed in the aftermath of the global financial crisis. This fresh look, focusing on simplification and supporting economic growth, is to be welcomed. Earlier concerns that it could lead to fragmentation of the international regulatory concordat have substantially dissipated following supportive comments from senior US officials regarding continuing active participation in the international regulatory bodies.

However, there remain concerns, particularly in Europe, that outstanding work streams may be addressed over different time frames globally. This, too, would lead to a fragmented framework with the risk of skewing financial market activity to where the capital support required is lightest. Such an outcome has to be avoided to prevent capital misallocation, and is particularly pertinent for traded markets activity. The best outcome remains early finalisation of what has already been agreed globally in principle, and a further agreement that remaining regulatory changes will be implemented in lockstep across the major jurisdictions.

Europe must not allow its financial capacity and capabilities to be diminished

Negotiations concerning the future shape of financial service provision as the UK prepares to leave the EU will undoubtedly be complex and time-consuming. The essential questions that have to be addressed are whether, at the conclusion of the negotiations, the economies of Europe will continue to have access to at least the same amount of financing capacity and related risk management services, and as readily available and similarly priced, as they have enjoyed with the UK as part of the EU.

On a highly positive note, we are encouraged that there has been no suggestion of weakening regulatory or supervisory standards anywhere in Europe in order to improve competitive positioning; this is equally essential to preserve the credibility and capacity of European financial markets.

Increased cooperation on tackling financial crime is essential

Tackling financial crime remains both a priority and a key challenge. We have made significant progress in detecting and preventing bad actors accessing the financial system but recognise this is a never-ending effort. Additionally, as digitalisation of commercial activity increases, the risks of confidence-threatening disruption and economic loss, not least from cyber attacks, are amplified. Technology, and in particular data analytics and machine learning applied to big data, will soon provide much greater capabilities to help us meet our objectives. What is also clear is that greater cooperation between the public and private sectors, together with a refresh of bank secrecy laws and regulation designed for a different age, would significantly increase the effectiveness of our joint efforts.

The good news is that there is increasing evidence of such discussions taking place. We should aspire to a unique digital identity for all participants in the financial system; a mandatory register of beneficial ownership of corporate and other non-personal structures in every country; and finally, enabling law and regulation to allow sanctioned sharing of customer information within institutions cross-border, between peer institutions, and between the industry and law enforcement services in pursuance of tackling financial crime. With enhanced public/private cooperation to combat financial crime, we could deploy the industry's considerable investment in this area much more effectively to the benefit of the societies we serve.

Outlook

In spite of geopolitical tensions and uncertainties, the major economic regions seem more synchronised in their growth trajectories than ever. Business investment is rising in the US and could expand further if promised tax reform can be delivered. Confidence is notably improving within the eurozone, with the prospect of structural reform in France, following the recent election outcomes, seen positively for future growth prospects. China's economic data also is evidencing resilience after a slower period, and against this backdrop China's financial regulators have taken the opportunity to tackle risks evident in both the traditional and so-called shadow banking systems. With careful coordination and calibration, these moves are positive for the economy. The UK is, however, showing some signs of slower growth as the inflationary impacts of a weaker currency, Bank of England caution over consumer indebtedness and uncertainties over the EU exit negotiations constrain consumer and business confidence and spending.

> 'We enter this period with confidence, given our geographical and business line diversification, and strong balance sheet'

The risks to economic growth remain concentrated around geopolitical events and political mis-steps. Additionally, the formidable challenge within Europe of negotiating both the terms of the UK's exit from the EU and the basis of the future relationship will dominate political agendas for some time, crowding out time for other policy considerations.

We enter this period with confidence, given our geographical and business line diversification, and strong balance sheet. On top of this, HSBC is served by an exceptional management team and 233,000 dedicated and talented colleagues.

For the past six and a half years, it has been my great privilege to lead HSBC's employees as Group Chairman. As I prepare to pass on the baton, I could not be more proud of what we have achieved together and I thank them on behalf of the Board, for the last time, for all their support.

Douglas Flint
Group Chairman
31 July 2017