

# HSBC 2011 Investor Day

## Group Strategy

Presentation by  
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This is actually the second time we've had an investor day. The first time was in 2007 which lasted for approximately two hours. Today, we've set aside a whole day, and I think it's important for us as a new management team to set out, in essence, what we intend to do with HSBC.

The financial strength of the firm you're very familiar with; our liquidity and our diversity protected us from some of the worst instances of the financial crisis, and in many ways ensured our share price was less volatile than others.

But the reasons for holding our stock in a crisis become less relevant in recovery and I think, in our view, we now risk losing ground to more agile competitors. Or, to put it another way, we're a very large firm that delivers significant profits, but we're complex and historically, we've struggled to tell a coherent story about why our shareholders should own us. And we hope that the start of these annual investor days and, with quarterly interim management statements, we'll be able to communicate more readily to you what we're actually trying to do with the firm.

So, today, I am aiming, really, to do five things, and we are trying to make an investor case here. We're trying to set out what our strategy is and then basically, talk to you about how we're going to improve our capital allocation and our costs and accountability.

**We're going to set out the distinct position for HSBC** and why we think we sit amongst some of the most powerful trends that are taking place in the global economies in the 21<sup>st</sup> century.

**We're going to be honest about the particular challenges that we face**, including our cost challenge and our ROE.

**We will hopefully articulate a clear strategy of what we're trying to do**, and why we will position HSBC to be successful.

**We should be able to give you confidence as to how the team will execute on this.**

**And we'll take you through in detail the framework we're going to use** to allocate capital, the type of things and programmes we'll put in place to address our cost base, and how we intend to keep the financial strength of a geographically-subsidiarised bank, which we think in the context of the regulatory environment is absolutely critical, but without the increased cost of wastage which arises when that structure becomes federal.

Now, I've no doubt about the scale of the challenge that we face, but I equally have no doubt about the ability of my team to deliver. The market should not expect a list of radical news items today, notwithstanding what's been trailed in the press, but rather an understanding of how we will run the firm, so we'll set out a framework, but we will also publish as we go into the detailed customer group and geographic presentations, return on risk weighted assets targets by country and by customer group, which is a first for us.

We'll set out clearly the cost saving target, and I'm also going to publish a scorecard against which I will be accountable, so when we come back in a year's time, having taken interim stages of review at the quarterlies, we'll be able to check the progress of this team against that scorecard.

**First of all I want to dispel a couple of myths and provide some context.**

And this is important because the strategy really sits around international connectivity and wealth creation and the connectivity goes to our network. I don't think our network has been well explained historically.

This is actually a picture of Mexican dollar issued by the Shanghai branch of HSBC at the end of the 19<sup>th</sup> century. This bank was set up in 1865 in Hong Kong and Shanghai to finance trade. It was set up to finance trade between Hong Kong and Shanghai, and France, the UK, Japan, India and the United States. Those are the original operations that were opened for HSBC, so this firm began as a commercial bank, and in fact, what we now call CMB is effectively the current manifestation of that trade finance, commercial banking core skill set. In fact, it was Commercial Banking that led to personal banking. Once you start banking individuals who have firms, you do their personal banking. As they get successful, you do their private banking. As those firms get bigger, and actually, there are several examples in Hong Kong of this, you eventually do their wholesale banking, their foreign exchange, their derivatives, their bond issues etc. So the heartland of HSBC is commercial banking.

Now, sometimes, we struggle to explain why we're in 87 countries and, as a result, we're unfavourably compared to some of our peers. And actually, I think this is because we have allowed the market to view HSBC through a retail banking lens. No doubt, this is reinforced by our marketing strapline, the world's local bank, and the fact that most analysts and most portfolio managers sit in the two markets where we actually have the scale to be a very profitable retail bank, namely the UK and Hong Kong, so they see our branch network all around them.

But actually, Commercial Banking and Global Banking and Markets, both of which have been built organically, contributed over US\$54 billion of profit before tax between 2007 and 2010, so during the height of the worst financial crisis since the 1930s. And they both rely on the network – the network of branches that we have and the position that we have in 80 plus countries. And I strongly believe that we do actually benefit from a network effect, precisely the thing that Metcalfe’s Law describes with phone networks applies to 87 countries with Commercial Banking and Global Banking and Markets, with significant clients in those countries.

As I say, historically, we’ve not actually projected Commercial Banking and Global Banking and Markets as the reason for the network. But actually, the network’s critical to both. Retail banking does not need the full network. It never did. And today, we’ll provide clarity as to how to think about retail banking in the future, and our plans to build a new wealth management business with a focused, precise set of personal banking customers. We’ll show you where it’s important and where it’s not.

Going forward, do not mistake the marketing strapline, ‘the world’s local bank’, for our strategy. So I’d ask you to look at our network and consider its values through the lens of Commercial Banking and Global Banking and Markets. And therefore the trends in world trade, GDP and demographics, which I will turn to shortly become immensely important and present a massive upside to this firm which we will capture. This firm has a terrific trading heritage. It sits with exposure to significant growth markets and actually, we have the financial resilience to deliver against those opportunities.

Let’s have a quick look at our share price. As I said before, we are a firm that produces significant amounts of profits, but struggles to tell a coherent story to our investors. So therefore, we have tended to be broadly flat against the market for actually the last 11 years. The share price has gone broadly sideways for 11 years.

We outperformed the market significantly, actually, for the prior period. Now, clearly our resilience through the crisis has been important to shareholders, and our dividend payments have also been important to shareholders. But, if you look at our dividend payments, we paid out US\$31 billion in the last four years. That makes us the second highest in the industry globally. ICBC is higher than us. But it’s equally clear that paying dividends is not enough because despite paying those dividends, the share price has essentially remained at £6.50. So we clearly need to articulate much better the growth story that HSBC can take advantage of and deliver to you as shareholders.

I think it’s also extremely important for you to realise that the senior management of the firm have substantial shareholding themselves in HSBC stock. Most of you are aware that I voluntarily have built up a substantial position in HSBC, but if the new LTIP is approved at our AGM, all of us in the top team will be long term holders of HSBC shares and unable to sell them until we retire. So we therefore believe that we’ve designed a compensation system that reinforces the alignment between management and long term shareholder interest and

we think that is actually extremely important. So what we hope to communicate today is both the long term vision, but also in the short term, some of the action steps we clearly need to take to progress along that journey.

**So, let me start to try and make the investor case for HSBC.**

Our strategy in essence is stored around two main elements. One is international connectivity. We have basically assumed that the major economic regions and financial hubs of the world, and the linkages that exist today in trade capital flows, will continue to grow. And I will talk about this in a little more detail in a moment.

We also believe that the rebalancing of the global economy, from the developed world to the emerging markets, will continue. Indeed, we believe that 19 of the 30 largest economies in the world by 2050 are ones that we today describe as emerging markets, but are also ones in which we’re positioned.

And we also believe that if you consider that the world’s connectivity will continue (and as I say, I will make the case as to why I think it will continue in a moment) and you believe that the highest growing markets sit in the emerging markets, but that the developed world would continue to trade with them, then we believe that you would also want to invest in those opportunities with a financial institution that has the hallmarks of financial strength, liquidity and capital that HSBC offers.

**Let me outline in a little more detail the macro trends that we think are at the heart of owning HSBC.**

**Trade will continue to grow.** Trade is forecast to grow between 2000 and 2020 by nearly nine percent per annum. The sources of these assumptions are in the footnotes. Now, this is an area of natural strength for HSBC, given our international network and given our trade finance heritage.

Imbalances will continue to drive international capital growth. By 2020, total global funding surplus is forecast to be US\$21 trillion. But actually, the most of that sits in Greater China, Japan, Germany and the UK. The UK will move from deficit to surplus during that period according to our assumptions.

The capital markets will enable economies to obtain the required financing, but if you look at this, it is impossible for countries to retreat from global capital markets. They just can’t fund themselves, so any notion that protectionism will end any of these kind of global connectivity arguments, I think, is implausible. It’s hard to see how the US can finance itself without being involved in global capital markets. There is a structural imbalance. That structural imbalance will exist for the foreseeable future. That structural imbalance offers capital, FDI and trade flows, which because of our geographic footprint, because of our network, we’re actually uniquely positioned to take advantage of.

**Having said that, the world is actually surprisingly concentrated.** If you dig into trade flows, 35 countries account for 90 percent of growth in trade flows over the next ten years, and that also holds true for external debt, bank profit growth, wallet available for bank profits and indeed, FDI.

So, actually, it's not about being in 200 markets. Again, I often find that one of the things being put to me is, "Well, if you're the world's local bank, you know, being in 87 countries isn't enough. Look at it from the other point of view." Actually, it's quite concentrated, but again, bear in mind the network's vital for Commercial Banking and Global Banking and Markets. But as you will see as set out, the individual geographic presentations, which will focus a lot on the growth opportunities and the customer groups, you will see that we are not going to try to be all things to all people in all markets.

**The other trend I think that is absolutely set in train is the rebalancing of the world economy.** Now, the centre of gravity continues to re-balance towards what are currently called emerging markets. By 2050, as I said earlier, we believe that 19 of the top 30 economies will be those currently deemed emerging markets, and these are all countries in which we already operate. The cumulative group will be massive and HSBC gives you access to that, and actually to the appreciation of their currencies.

The key thing about the fact we've been in the places a long time – and this is incredibly true about Asia Pacific, about the Middle East, about Latin America – is that trust and relationships are at the heart of business. These are not parts of the world that have institutionalised their business processes in the way the United States and to some extent, the European Union has.

Having said that, the developed markets will not become irrelevant any time soon, and it's really not a simple zero-sum game here. Many developed markets remain incredibly important, both as trading economies and as centres of wealth. The key point, therefore, is that we will continue to sit in both the developed world and the emerging markets. We do not believe it offers the full opportunity to simply become an emerging market bank. Our European business is actually incredibly important to us.

If I could just step back for a second, to over-simplify the world, there are four big economic blocks. There's Japan, the United States, the European Union and the emerging markets that are in essence driven by China. We have substantial presence in the emerging markets, driven by China. We have a substantial presence in the European Union. We need to stay in both so that we can involve ourselves both in the emerging market to emerging market trade flows and wealth flows and capital flows, and the developed world, European Union to emerging market flows. Every time that I go and meet the CEO of a major corporate in France or Germany, they're investing and they see their growth opportunities in exactly the same markets that we have a footprint in.

**As this economic shift takes place, there will also be a substantial change in where the wealth creation takes place in the world,** which is partly what our wealth strategy is about.

You can see in the middle graph those markets expected to have a GDP per capita above US\$35,000 by 2050, and the reason I've chosen that level of US\$35,000 per capita is that's the current GDP per capita of Hong Kong. The reason I say that is to illustrate an incredibly important point. The power of income per capita growth can drive bank profits.

Over the past 40 years, GDP per capita in Hong Kong increased 31 times from US\$900 a head to US\$31,000 and our Group profits, just in the last 18 years have increased seven times. You as analysts and owners are aware of the extent to which Hong Kong has driven HSBC's profit growth, so if you look at where the potential new wealth creation is and just look at the multiples of growth of income in places like China, India, Mexico, Brazil, Turkey, you can see that wealth creation in the emerging markets will be a fast growing phenomenon that will take place over the next five, ten years. And again, we have access to those clients and therefore, give you as investors access to that opportunity.

But, we do believe that the best vehicle to express this through is one that has the type of financial profile that did enable us, for want of a better expression, to have a good financial crisis. In other words, we have deliberately created a business that's diversified by customer group and diversified by geography and actually has an A/D ratio substantially below 100. We've given guidance that 90 is the ceiling (we actually at the first quarter reported that our number was 78.2) and we are not going to change that.

We think it's incredibly important to have retail deposits in order to not find yourself in a situation that happened to a number of our competitors. I think we'd all recognise that a number of competitors actually ran out money as opposed to running out of capital, so if you're reliant on the wholesale market, you're reliant on a massive sentiment shift that can take place very, very quickly. This is critical. We continue to have a substantial surplus of deposits over loans and that will remain the case.

**Our geographic diversification is important to us.** This will continue, by definition, given that these economies in the emerging markets are faster growing, and continue to shift the balance sheet towards the emerging markets. But we are not going to pull back in the UK, France and Germany, any time soon because we reckon they are incredibly important to the connection between the developed world and the emerging markets and I'll talk a little bit more about that in a moment as well.

Our financial strength also has enabled us to deal with some pretty hairy problems which we were able to take care of ourselves internally without resorting to any government equity or debt from any government anywhere in the world. And that, frankly, has been a very real stress test, so the financial strength of the firm to manage its way through both the sub-prime problems of household and actually the SIVs

and conduits in global banking and markets. I think it's proof of concept of the financial resilience of the firm.

**Now, clearly, to deliver against this in a meaningful way short term for you as shareholders, we have to improve some things quite substantially.**

**We've got to improve the way we deploy capital.** As Douglas said, our tier one ratio, we believe as a global SIFI, will be between 9.5 and 10.5 percent under Basel III based on the information today.

At the moment, we delivered a 9.5 percent return on equity in 2010, and we set guidance of 12 to 15 percent. Now, that guidance of 12 to 15 was based on a bottom-up calculation of return on risk weighted assets by customer groups and geography applying Basel III to get to that return. So although I've seen this morning on some of the newswires the view that 12 to 15 is too low, we only set it two months ago, and it was done with quite a lot of mathematical science. And I can assure you, if we manage to get outside the top end of it, we will be equally delighted. But the 12 to 15 is quite carefully calculated and thought through and Iain will talk a little bit more about this in his presentation. But we are going to be hard-nosed. We're going to be disciplined about the way we allocate capital.

**We also need to do something about our costs.** We clearly have a cost problem and I will talk in a moment about the programmes that we've put in place to bring costs down. And we obviously do need to get the ROE of the firm up. But as a number of you pointed out after the results, on the one hand, there's a group that thinks 12 to 15 is too low. On the other hand, at 9.5 we're US\$4 billion short of getting to the 12 with our 2010 numbers, so there is a challenge in there marching towards those numbers in any event. But we will deliver towards this, and this team will address the issues of the firm with some energy.

So, having described our distinctive position, let me move to the right hand side of the slide.

**I'm now going to set out our strategy and explain why you should be confident that we will execute against it.**

There are three key elements to the execution part; clarity of vision; more efficient capital calculation (and I'll set out the strategy and how we will make capital allocation decisions both now and on an ongoing basis); and the action plan to deliver the cost and accountability.

As Douglas has said, I've actually made 24 changes since I became Group CEO on 1<sup>st</sup> January. The important thing about those is that this is a refreshed and new team who are going to act cohesively to drive this forward. But also, most of these came from inside, which shows the bench strength that this firm has built up and I actually think is a tremendous strength of the firm.

Rightly, ultimately, the responsibility for delivering this strategy will fall on me, which I'm perfectly comfortable

with, and as I say, we will set out a scorecard for which I'm perfectly prepared to be held accountable at the end.

**So what is the strategy of the firm? The goal is to be the leading international bank.**

This is a really important slide so we need to spend a bit of time on this. There are two main elements to what will drive the future shape of HSBC and its strategy.

**One is this international connectivity point, the case being made by the macro trends that I showed you earlier.**

It's therefore important that we continue to have a substantial network, because the way you take advantage of this is through Global Banking and Markets and Commercial Banking, and, to be crystal clear, to be the leading international bank is a goal. It's not a marketing strapline. It's not a piece of jargon. It's a goal. It's also a realistic ambition and it forces us to take a sharper focus on what we're actually doing, so presence in key markets matter for international connectivity. If you accept all those trends about trade, capital flow, wealth creation etc, you need to sit across those geographies where the considerable economic growth will take place in the next several years, and we do.

**The second thing that we're going to focus on is that we will now limit Retail Banking only to where we can achieve scale as a full-scale retail bank.**

This means that we're going to segment, and Paul will talk in detail about this, our Retail Banking operations and categorise them very, very specifically into different-sized opportunities.

Large scale positions such as Hong Kong and the UK have profitability, have scale. There are some very high growth markets which we will continue to invest in like Mexico, Singapore, Turkey, Brazil. There are some very small countries actually which are just fine like Panama and Malta. The USA is a specific issue that I'll come back to a bit later. Then, there are countries we need to invest in for the future like India and China, but actually India's PFS business has not been particularly successful and that's one of the reasons that we took RBS's network there. It's part of a restructuring exercise that needs to take place. You'll then find we're left with about 39 countries that don't fit into any of those parameters, and Paul will talk a little bit more about that.

There's a second thing, though, that goes on within this area, which is effectively the growth of a Wealth Management business and I'll come back to that in just a moment. But these two big drivers; the network effect which sits across international connectivity for Commercial Banking and Global Banking and Markets; and the need to reposition Retail Banking and the wealth creation sphere.

Two big blocks with effectively Commercial Banking and the network in the first and the restructuring of Retail Banking and Wealth in the second.

**So, how are we going to decide how we use the money?... and this I think is really, really important.** We've already introduced a process that internally we simply call five filters. We need to improve the way we deploy capital to achieve this profitability target of 12 to 15 on equity by 2013, and we've already launched a review of our businesses, assessing each one based on these five filters.

The first one, not surprisingly is international connectivity. Does this country (and do the businesses in this country) trade and connect with any other country that we're involved in any meaningful way, or is it totally standalone so there's no connection whatsoever? A totally standalone business would be US Household, with no connection whatsoever to any other customer group of HSBC.

Number two, is it in a country whose economy will matter over the next 20, 25 years or is just a small country that frankly will still be a small country, or is it one that actually is going to really be part of the global growth story?

Having established that, we then dig into the second set of filters - are our current returns attractive?

So number one, do we have a decent ROE that's in the 12 to 15 range?

Number two, is the cost efficiency ratio in the 48 to 52?

And number three, does it fund the Group?

My earlier point was about the deposit base being incredibly important: we might have a country that was having difficulty on the first two, but was a huge source of deposits to the Group. It would need to be a huge source of deposit for a G3 currency because we actually run our liquidity by currency group silo, but it's possible that that may happen.

So, you can therefore see the way the filters will work. If you dig into a country that's highly connected and will really, really matter - and say that's France - when you dig into that and you decide that in fact some of the profitability and efficiency measures aren't quite there, then that's one that you're going to turn around and improve. You need to do some restructuring work. It's critical. Its connectivity's there. It's going to be in the top 30 economies in the world, but the numbers just aren't there. It needs some work on it.

If you look at one that has high connectivity and economic development and all three are there, then you're going to invest, and actually an example of that is the build out in Germany of our Commercial Banking business which we've started to do. Germany is the only OECD country that's grown its share of world trade over the last 15 years. Equally, we continue to invest in Turkey and in Brazil for exactly the same reason; all five boxes work.

When you look at some other countries, they are medium or low in terms of their connectivity to the rest of our network, or indeed, their economic relevance at any point in time. So if actually they happen to drive high achieving profitability, efficiency and liquidity, then we may well continue as we

are. Panama and Malta would be examples of those. They don't hit the strategic relevance, but actually their ROE, their cost efficiency ratio and their A/D ratio are perfectly satisfactory.

Then there's a bottom set that aren't going to hit any of these. They are low in terms of their strategic relevance and they're just not delivering the freight, and in those, we're going to have to decide whether we can absolutely turn them around, which in most instances is very unlikely to be the case, or we're looking effectively at disposing of them or shutting them down. And there's a live example of some of this work already happening, which is the exit from Retail Banking in Russia.

Now, as I said, we're not going to announce a whole set of these today for rather obvious reasons. But if you look at the five filters, you can kind of work out directionally where this is going to go, and what you will be able to do is when we do make announcements, refer back, so you can actually see there's a logic and a framework to how we're driving forward the allocation of capital in order to get to the 12-15% return.

Now, costs... and this is really, really important.

**We have stated here today we're going to take out US\$2.5-3.5 billion of sustainable cost saves over the next three years.**

It's going to take a while to do this because it requires us to re-engineer a bank that's been run as a reasonably loose federation. It's also going to take a while because it's actually just a very large firm. But clearly, if we can deliver this sooner than this we will, but the US\$2.5-3.5 billion we're confident we can deliver.

Now, it's really important to focus on the fact that this will be driven through four different main programmes and I will talk a little bit about each. In order to make sustainable saves, we have to look at re-engineering our business, rather than the traditional HSBC way of managing costs which has generally been to cancel the newspapers, being incredibly mean about travel and, you know, restricting people on how much laundry they can put into a hotel on a business trip. We really, really need to look at a substantial re-engineering of how we approach things. It takes an awful lot of socks to get to US\$2.5-\$3.5 billion, so we really, really do need to look at a couple of things.

We do not have consistent business models in what was called Personal Financial Services and now is called Retail Banking and Wealth Management. That means, therefore, that we have multiple propositions, we have multiple marketing groups, and for example, as a result of that, there's multiple demands on IT to write systems with huge amounts of local idiosyncrasies in them which clearly puts up the costs.

That's another reason why I put Paul in charge globally of Retail Banking and Wealth Management. Prior to Paul being appointed, there was no single global head of PFS, and therefore, you got this immense local richness and colour

which hugely increased our cost base, because you've got multiple product propositions, and multiple system deliveries that have to take place.

Although it's less pronounced in Commercial Banking, it would also be true in Commercial Banking that we don't have one single business model. One of the reasons why Global Banking and Markets has a cost efficiency ratio of 49, is it does have one business model because it's been run as a single global business now for a very long period of time.

The second thing we're going to need to do is to streamline some of our IT processes. We have compounded the challenge of our IT costs, as I say, by not designating a very, very defined consistent target operating model for PFS and CMB which has made the IT challenge harder for our IT colleagues. And, as Sean will talk about, we look pretty good because we've now benchmarked ourselves, using some external consultants, on the cost of our IT function in terms of running the bank on a day-to-day basis. But in terms of software development and development of new systems, and partly for the reasons that I've just outlined, we don't look best in class. So there's some work that needs to take place there.

We also need to look at our regional head offices. We have a whole lot of multiple head office and control structure that come about as a result of being organised by customer group, geographies, regional head offices, legal entities. There's work going on again, and it is true that we have brought in Boston Consulting Group to help us look at what's best in class in this regard, at de-layering, and Iain and Sean will take you through these. But as I say, there are some very clear things that we need to do to drive this forward.

**Let me talk a little bit now through the customer groups and the countries** and then I'll pass on to Iain to talk you through the financials.

So, let's look at how we'll execute this strategy in each customer group.

**I'll start with Global Banking and Markets.** Clearly, the key challenge here is more capital is applied against the business as we go to Basel 2.5 and Basel III. We're going to have to work harder to deliver target returns. But the other thing I really believe, actually, having run this business for a very long time, is we need to do a much better job of explaining to you the nature of our customer facing Global Banking and Markets business outside of Balance Sheet Management.

At present, this business attracts about the same P/E ratio as BarCap and Deutsche Bank, but it's actually a very different business. It's client facing. It's involved in traded liquid markets, and it has an unparallel capability in emerging markets which we believe strongly is the major growth engine for the world.

This business has been grown organically. It's produced US\$30 billion of PBT during the last four years when many of our competitors actually were loss making. And what's

also happened, and Samir may well talk a little bit about this as well is, we think we've re-established a base line for this of about US\$9-10 billion of PBT. Pre-crisis, this thing ran at US\$5-6 billion, which tends to evidence that we've probably captured a sustainable market share advantage during the financial crisis.

**Commercial Banking:** as I said before, this is the absolutely the heartland of HSBC. This is the DNA of the firm. It always has been and always will be a massive jewel in the crown for HSBC which has incredibly high barriers to entry and the reason it has high barriers to entry is, you need the network I described earlier to do this. If you want to be relevant to a manufacturer in France or a small manufacturer in the UK who's looking to do business in Argentina, you need to be in Argentina. It's no good being in Birmingham and helping them from there. You need to be in both places, so the network effect creates a massive entry level barrier to this. And we believe strongly that global trade will continue to grow and these kinds of trends are in place.

This business already has a cost efficiency ratio within the group's target and Alan will talk about return on risk weighted asset targets that we're moving to.

**We've renamed Personal Financial Services as Retail Banking and Wealth Management** and actually there is significance to this. I know there's a deep cynicism about large institutions renaming things, but let me explain why we have renamed things.

First of all, there's two distinct pieces here. There is a new business which is building out Wealth Management because we do think the trends that I set out at the start of the presentation offer huge potential for HSBC. It's going to be focused. Paul will focus effectively on 18 markets, not on 87 markets, where we believe that the opportunity is the biggest to deliver Wealth Management. But we do think that actually this Wealth Management opportunity works for us, because we're in the emerging markets which have got the fastest wealth creation. They have the highest savings rate of any countries anywhere in the world, but actually, even in Europe, there are significant unfunded government pensions which means people will have to save for their own retirement which will again create a catalyst for the contractual savings industry – which is actually what nearly all of us work in. So we can see both in Europe and in the emerging markets, a considerable growth, therefore, for Wealth Management.

**Retail Banking:** think of this separately, it needs to be segmented, and as I said earlier, you've got evidence of what we will do when we discover a sub-par retail portfolio. We'll exit it, which is just what we did in Russia, so Paul will take you through in detail how we'll look at the various different countries. As I say, this has been renamed, but it's not a form over substance. It's been renamed to make it very, very intellectually clear to you there's a Wealth Management strategy which involves insurance, asset management in about 18 countries and there's a restructuring of our extant Retail Banking businesses which will take place at the same time. Don't mix them up.

**In Private Banking**, it's the same point as Wealth Management. This should be a massive growth business for HSBC. We are sitting in the fastest growing wealth creation in the world. That sits obviously in Latin America, in Asia Pacific and in the Middle East, and actually we have a brand that's trusted, and therefore, this is a natural extension of what I said earlier. If you think back to Commercial Banking at the hub, if you've built your own business as an owner/manager, and you eventually list it, you have that wealth event that creates the Private Banking opportunity and actually, an awful lot of the Private Bank referrals as Chris Mears will talk about, come from actually within HSBC.

Now geographies. This is very, very important.

**We have a business in North America that is run off in respect of Household, but we do not believe that just letting Household run off gives us a strategy in the United States.**

We also believe it's absolutely critical to remain in the United States. The US is still the biggest source of investable funds and is still the world's largest economy, so we have absolutely no option but to be in the United States. It's also the case that the US dollar is the world's reserve currency and the main payment currency in the world.

What we need to do is to re-position our business to be relevant to the United States, and let me talk, first of all, a little bit about the end vision and then about some of the restructuring action that will take place.

The only way that we can add value in the United States is actually by connecting into the other countries in which we operate. We can't compete on a domestic agenda in the US against the four big American banks that have got much bigger. So the opportunity lies in Global Banking and Markets, but connecting that in America. The opportunity lies in Private Banking domestically onshore, but also with Latin American clients. The opportunity – and this is the new focus actually – lies in Commercial Banking and fits also with the fact that the US (there's some interesting work that the Brookings Institute has done on this) is rebuilding its manufacturing industry and looking to expand its export and trade, and it's trade where we have the expertise. It's trade where we bring something to American clients that actually, we genuinely believe we have more skills in than the American banks, and so the branch network needs to be repositioned, therefore, to fit where the renaissance of US manufacturing will take place.

We also believe the US will probably have some of the cheapest energy sources of any country in the world as it starts to fully bring out its shale oil and gas. Therefore, actually, we are quite bullish on the US economy and quite bullish on the manufacturing opportunity, so therefore we have started a strategic review and I'll let Niall talk about it in detail.

No decisions have been made as yet. But we have started a strategic review, and within that the card business is not strategic. Go back to the five filters. Those are store cards

and subprime or exiting. With store cards you don't get to the client so there is no cross-selling opportunity. It is not strategic to us. However, we have lots of capital and lots of liquidity, so we're also not a forced seller. But if we're going to be disciplined about the five filters, we need to look at this, and Niall will talk a little bit about this, and also some upstate New York branches that don't fit with where we think the growth opportunity in the US economy is.

**Turning next to Latin America, the big focus for us is Brazil, Mexico and Argentina.**

These are the three countries we want to focus in on. In Brazil and Mexico alone, there will be 35 million people moving into social-economic groups A, B and C by 2014. So again, there's a substantial Wealth Management opportunity there. There's also a substantial Commercial Banking and Global Banking and Markets opportunity – and we already have (which Samir will talk about) a strong Global Banking and Markets capability in Latin America.

We have, however, a problem here where our ROE is below the local market and our cost efficiency ratio is higher than the local market. Emilson will talk in detail about this, but a lot of this has been about regional headquarters. And the restructuring charge that you saw come through in the first quarter actually relates to removing some of the cost base at the regional headquarters in Mexico City. So, we accept the fact that we need to do something – more than something. We need to sort out the ROE here, and sort out the cost base, but this remains, in terms of those countries, Brazil, Mexico and Argentina, an absolute top priority which do hit the five filters and we will continue to connect them to Europe.

**As I said earlier, it's crystal clear to me that we must remain fully invested in the UK, Germany and France to drive Commercial Banking and Global Banking and Markets.**

If we really want to capture the flow between the developed world and the emerging markets, so called North-South, we have to have a credible presence in those countries.

It's absolutely the case (and Andreas Schmitz, who runs our German operation, is at the back of the room) that if we want to do business with Volkswagen in China, we need to cover them with German colleagues out of Dusseldorf, covering them in Wolfsburg. It just works that way. The same is true of major French clients and Christophe de Backer is also in the room who runs our French bank. So to be crystal clear, the UK, Germany and France are key to Commercial Banking, and Global Banking and Markets.

The UK is absolutely essential to Retail Banking, and by the way, the UK retail bank cost efficiency ratio is not the worst in the industry. Actually, if you look at it, and you'll all understand this, there's an absolute inverse relationship between A/D ratio and cost efficiency ratio because interest rates are at 50 basis points. A bank with a low A/D ratio at the moment has a high cost efficiency ratio because it has no net interest margin on its deposits. So if you map it out, the guy with the worst A/D ratio has the best cost efficiency ratio

because obviously he's borrowing from the Central Bank or the market at 50 basis points. It's completely inverted. A better way to look at it, I might suggest, is to look at cost per branch and in that regard, we're completely competitive.

It is the case, though, across Continental Europe, that we need to do something about our cost base, and this again, is an area where we've got multiple layers of head offices. Actually in this building, there are two head offices. There's another one in Paris. There's one in Geneva for the Private Bank. There's one in Dusseldorf for the German bank and we have brought in Boston Consulting Group, again to try and get us to a position where we can see who's best in class, and what the journey would be to get towards best in class.

**The Middle East and North Africa:** obviously a very troubled part of the world in the first quarter of this year. Indeed, in the first quarter of this year, we've obviously had very sad developments in a number of countries in terms of loss of life in this part of the region. We've been here for 50 plus years. It's a core part of HSBC's DNA again. In fact, the original two banks are the Hong Kong Shanghai Banking Corporation and the British Bank of the Middle East, so we remain completely committed to the region.

You know, it has got 61% of the world's oil reserves. It has got 45% of the world's gas reserves. It has got a population, excluding Pakistan and Iran, of 265 million and actually, it has got also a huge source of investable funds sitting in its sovereign wealth funds. So we actually think that this is a great business. It's going to go through a turbulent period because of political instability and there will therefore be some headwinds on revenue which are unavoidable. But if you want to talk about long term, this is the kind of place where HSBC's sticking power and staying power always gets rewarded when the good times return.

So this is a business which Simon Cooper, who is here, will talk to you in detail about, but it is one that we remain very, very committed to.

**And, then last, the most important region for HSBC without any doubt: Asia.**

This is the heritage of the firm. This is the history of the firm. Now, we have the potential here not only to connect the key economies with each other, but also with the rest of the world. This is our heartland and it's an area where we face significant inflationary wage pressures which I talked about on Monday and everyone's woken up to the fact that this is where the growth is.

We're now working to get a grip on cost. But we're not going to compromise on paying for talent, so this means managing down non-staff costs. And it means, again, that those four big programmes, to take the US\$2.5-3.5 billion out, have significance even to Asia Pacific where we have some of the best cost efficiency ratios in the Group, because Peter faces considerable headwinds in terms of wage price inflation. You'll have seen that again in our first quarter IMS statement.

The two massive priority markets are obviously Greater China and India, and maintaining leadership in Hong Kong, and China as the top foreign bank, will help us to be number one in RMB – and the internationalisation of the RMB is a huge opportunity for this firm. We will defend our leadership positions in Hong Kong at all costs. You have to accept that. This is the heartland of the firm and we will do so, and so therefore, there will be wage price inflation. There will be cost price inflation there.

Our strategic investments in China have performed incredibly well, as with Ping An, for example, and we will continue to expand our BoCom partnership. We are at the moment studying a joint venture where we will look to work together with Chinese SOEs as they come overseas, with BoCom providing the China side of it, and our network overseas providing the international linkage. To be clear, none are for sale. We wish to maintain our level of exposure. Let's be clear here. We wish to maintain our level of exposure and commitment to China and these investments are, for now, the best way to achieve this.

India is also an incredibly important market to us. We will grow our business out in India at the pace that the regulators allow us to. The reason we took RBS's business is that gave us access to a number of branches that would have taken us years to get on a case by case basis.

**Now we, as a management team, all accept that we're accountable to you for delivering this.**

We're accountable to you to getting the ROE sorted out, getting the cost efficiency ratio sorted out and delivering on this strategic plan. Most of the Group Management Board will actually present to you today. The delivery, I know, depends on execution, and you are going to have to judge our ability to execute on this, and execution will be delivered by the Group Management Board under my leadership. At the end of the day we're all accountable and obviously I have primary accountability.

I've also brought together, so that you can meet them during the lunch break and during the coffee break, other members of the senior management team (and actually during the Q&As). You've got all the bios in your booklet and I want them to have exposure to our owners and to the sell-side analyst community.

**I also mentioned briefly the importance of values in the execution of our strategy and right at the heart of this is an expectation that every employer will act with courageous integrity.**

Some of you may have picked this up, but we started a big piece of work to define the way we do things at HSBC. We have clearly a very large institution. If I'm going to de-layer – and if I'm going to empower and decentralise and move from what's been a command and control culture, which is the origin of HSBC's culture – then we need to set out a series of values and principles that define the way we behave here. We need to be certain that we can delegate, with confidence, that the kind of outcome that will take place

results in ethical behaviour and writing the type of business that we can be proud about.

So this courageous integrity again is not some happy-clappy strapline. This will be the basis on which we evaluate people. As well as every one of my senior team's score cards having ROE goals, cost efficiency goals, they will also have a rating in terms of their behaviour and the values, defined by courageous integrity with three further things that fold out underneath it which are dependable, open and connected. We're actually doing values training for the top 300 people in the firm because again, to galvanise and motivate and drive a firm like this, it needs more than one person. It needs more than 12 people which is a Group Management Board, so we're cascading that down.

So, in summary, I think we have quite a distinctive position. I think we do sit across some of the major trends that are taking place in the world and there's two ways for us to deliver that to you.

One is through the network which is Global Banking and Markets and Commercial Banking.

The other is to drive forward a Wealth Management business and at the same time, we need to restructure our Retail Banking.

We clearly need to deal with our ROE and allocate capital in a hard-nosed disciplined way going forward, which clearly hasn't always been the case in the past. And let's be clear, the reason it hasn't been the case in the past is, we've always had massive amounts of surplus capital. It is only in a world that's moved towards Basel III that capital actually for HSBC has become a scarce resource. It is also probably the case that the federal structure enabled some inefficiencies to persist for longer than they otherwise would have done. And the third reason why it's probably not been possible to do this before is we were in the worst financial crisis since 1930. So the reason we're looking at it now, is because we can look at it now and we need to look at it now.

As I said, this is a firm that's consistently delivered huge amounts of revenue, but has struggled to explain its investor case to people, to make the case as to why HSBC is a stock that you should believe has growth potential. And, as I say, to be absolutely clear, we're going to take a rigorous, relentless approach.

We will be more disciplined on capital allocation.

We've got a programme in place that's already started to cut costs, and the management team accept they're accountable to you for delivering the result.

So this is an outline of a report card, and I'll talk a little bit more about this at the end of the day, but this is essentially what I'm prepared to be measured on and held accountable for, to execute against over the next two years. We clearly, each quarter at the IMS, will be checking back to this kind of stuff. It's quite possible that actually, if we made progress into these earlier than that period of time, we will revisit it and flex it to a more aggressive position.

But again, I want to give you some sense, quite clearly, of the fact that we as a team have a sense of urgency about the need to do this, have a sense of the need for intensity and are now, going forward, going to be much more transparent and open with you, the investors and the sell-side analysts, about what's going on here and what our ambitions are.

I will now hand over to Iain.