HSBC

HSBC Bank Capital Funding (Sterling 1) L.P.

(established in Jersey as a limited partnership under the Limited Partnerships (Jersey) Law 1994)

£700,000,000
5.844% Non-cumulative Step-up Perpetual Preferred Securities

having the benefit of a subordinated guarantee of

HSBC Bank plc

(incorporated with limited liability under the laws of England and Wales with registered number 14259)

Issue Price: £1,000 per Preferred Security

The £700,000,000 5.844% Non-cumulative Step-up Perpetual Preferred Securities, (the "Preferred Securities") each issued for a capital contribution of £1,000 (referred to herein as the "nominal amount"), representing limited partnership interests in HSBC Bank Capital Funding (Sterling 1) L.P., (the "Issuer"), will be issued on 5 November 2003 (the "Issue Date"). The Preferred Securities will entitle investors, subject to certain conditions described herein, to receive non-cumulative cash distributions ("Distributions") annually in arrear on 5 November in each year until 5 November 2031 and thereafter semi-annually in arrear on 5 May and 5 November in each year. Distributions shall accrue from (and including) the Issue Date to (but excluding) 5 November 2031 at a fixed rate per annum of 5.844% and semi-annually in arrear from (and including) 5 November 2031, at a floating rate per annum equal to the sum of 1.76% and six-month LIBOR for the relevant Distribution Period (as defined herein). The first Distribution will, if payable, be paid on 5 November 2004, and will be calculated in respect of the period from (and including) 5 November 2003 to (but excluding) 5 November 2004). See "*Description of the Preferred Securities – Distributions*".

The Issuer is a Jersey limited partnership and is not a legal entity separate from its partners. All obligations of the Issuer to make payments in respect of the Preferred Securities are guaranteed on a subordinated basis pursuant to a guarantee dated 5 November 2003 (the "Guarantee") given by HSBC Bank plc (the "Bank"). See "*Description of the Guarantee*".

The Preferred Securities are perpetual securities and not subject to any mandatory redemption provisions. The Preferred Securities may be redeemed, at the option of HSBC Bank (General Partner) Limited, a wholly owned Jersey incorporated subsidiary of the Bank, as general partner of the Issuer (the "General Partner"), on 5 November 2031 or on each Distribution Date thereafter, in whole but not in part, at an amount equal to the Optional Redemption Price, subject to satisfaction of the Redemption Conditions (each as defined herein). The Preferred Securities are also redeemable, subject to satisfaction of certain conditions, in whole but not in part, at any time following the occurrence of a Tax Event or a Regulatory Event (each as defined herein). Under existing regulations, neither the Issuer nor the Bank nor any of its subsidiaries may redeem or purchase any Preferred Securities unless the Financial Services Authority, or any successor organisation thereto in the United Kingdom (the "FSA"), has given its prior written consent. See "*Description of the Preferred Securities – Redemption and Purchase*". These requirements and restrictions do not affect the ability of the Bank and its subsidiaries and affiliates to engage in market-making activities in relation to the Preferred Securities.

In the event of the dissolution or winding-up of the Issuer, holders of Preferred Securities will be entitled, subject to satisfaction of certain conditions, to receive a Liquidating Distribution (as defined herein). See "*Description of the Preferred Securities – Liquidating Distributions*". Upon the occurrence of a Substitution Event (as defined herein) or, subject to certain conditions, at the option of the General Partner following a Tax Event or Regulatory Event, the Preferred Securities may be substituted by the Substitute Preference Shares (as defined herein). If any Preferred Securities are outstanding on 5 November 2048 and no notice to redeem such Preferred Securities on or before 5 November 2048 has been given, the Preferred Securities will be substituted by the Substitute Preference Shares. See "*Description of the Preferred Securities – Substitution by Substitute Preference Shares*".

The Preferred Securities are expected to be assigned on issue a rating of A by Standard & Poor's Ratings Services, a Division of The McGraw Hill Companies, Inc., A1 by Moody's Investors Service Limited and AA- by Fitch Ratings Limited. A credit rating is not a recommendation to buy, sell or hold securities and may be subject to revisions, suspension or withdrawal at any time by the relevant rating organisation.

Application has been made to list the Preferred Securities on the Luxembourg Stock Exchange (the "Luxembourg Stock Exchange").

See "Investment Considerations" for a discussion of certain factors that should be considered by prospective investors.

The Preferred Securities have not been, and will not be, registered under the United States Securities Act of 1933, as amended (the "Securities Act") or any US State Securities Laws. The Preferred Securities are being offered outside the United States by the Managers (as defined in "*Subscription and Sale*" below) in accordance with Regulation S under the Securities Act ("Regulation S"), and may not be offered or sold within the United States or to, or for the account or benefit of, US persons except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act.

The Preferred Securities will be evidenced by a single global certificate in registered form (the "Global Certificate") registered in the name of a nominee of, and deposited with, a common depositary for Euroclear Bank, S.A./N.V. as operator of the Euroclear System ("Euroclear") and Clearstream Banking, société anonyme, Luxembourg ("Clearstream, Luxembourg"). Definitive certificates evidencing Preferred Securities will only be available in certain limited circumstances. See "*Summary of Provisions relating to the Preferred Securities in Global Form*".

HSBC

Global Co-ordinator, Lead Manager and Bookrunner

ABN AMRO **Credit Suisse First Boston**

Citigroup **JPMorgan**

Merrill Lynch International

Dated: 31 October 2003

The General Partner, acting on behalf of the Issuer, accepts responsibility for the information contained in this document (other than the Bank Group Information (as defined below)). To the best of the knowledge and belief of the General Partner (which has taken all reasonable care to ensure that such is the case) the information contained in this document is true and accurate in all material respects and is not misleading, the opinions and intentions expressed in this document are honestly held and there are no other facts the omission of which makes this document as a whole or any such information or the expression of any such opinion or intention misleading. In addition, the Bank accepts responsibility for all information contained in this document set out under the sections entitled "Capitalisation of the Guarantor", "Description of the Guarantor", "Recent Developments of the Guarantor", "Description of the Guarantee", "Description of the Substitute Preference Shares" and Annex A – HSBC Bank plc 2002 Annual Report and Accounts and the documents incorporated herein by reference (together, the "Bank Group Information"). To the best of the knowledge and belief of the Bank (which has taken all reasonable care to ensure that such is the case), the Bank Group Information is in accordance with the facts and does not omit anything likely to affect the import of such information.

The term "the Bank Group" has the meaning given in "Description of the Preferred Securities". Any reference in this Offering Circular to an action taken by the Issuer shall be taken to mean an action taken by the General Partner on behalf of the Issuer.

Neither the Issuer nor the Bank has authorised the making or provision of any representation or information regarding the Issuer, the Bank or the Preferred Securities other than as contained in this Offering Circular or as approved for such purpose by the Issuer and the Bank. Any such representation or information should not be relied upon as having been authorised by the Issuer, the General Partner, the Bank or the Managers.

Neither the delivery of this Offering Circular nor the offering, sale or delivery of any Preferred Securities shall in any circumstances create any implication that there has been no adverse change, or any event reasonably likely to involve any adverse change, in the condition (financial or otherwise) of the Issuer or the Bank since the date of this Offering Circular.

Prospective investors should inform themselves as to the legal requirements and tax consequences within the countries of their residence and domicile for or of the acquisition, holding or disposal by them of Preferred Securities and any foreign exchange restrictions that might be relevant to them. This Offering Circular does not constitute an offer of or an invitation by or on behalf of the Issuer or any of its partners, or the Managers to subscribe for or purchase any of the Preferred Securities.

Investors should satisfy themselves that they understand all the risks associated with making investments in the Preferred Securities. If a prospective investor is in any doubt whatsoever as to the risks involved in investing in the Preferred Securities, he should consult his professional advisers. This Offering Circular does not constitute investment advice or a recommendation to buy, subscribe for or underwrite any Preferred Securities by the Issuer or any of its partners, the Bank or the Managers.

EACH PURCHASER OF THE PREFERRED SECURITIES MUST COMPLY WITH ALL APPLICABLE LAWS AND REGULATIONS IN FORCE IN ANY JURISDICTION IN WHICH IT PURCHASES, OFFERS OR SELLS THE PREFERRED SECURITIES OR POSSESSES OR DISTRIBUTES THIS OFFERING CIRCULAR AND MUST OBTAIN ANY CONSENT, APPROVAL OR PERMISSION REQUIRED BY IT FOR THE PURCHASE, OFFER OR SALE BY IT OF THE PREFERRED SECURITIES UNDER THE LAWS AND REGULATIONS IN FORCE IN ANY JURISDICTION TO WHICH IT IS SUBJECT OR IN WHICH IT MAKES SUCH PURCHASES, OFFERS OR SALES, AND NONE OF THE GENERAL PARTNER, THE ISSUER, THE BANK OR THE MANAGERS SHALL HAVE ANY RESPONSIBILITY THEREFOR.

Investors in the Preferred Securities will be deemed to have represented that they do not own, directly or indirectly, 10% or more of the ordinary shares of the Bank. If at any time the General Partner becomes aware that an investor in the Preferred Securities owns, directly or indirectly, 10% or more of the ordinary shares of the Bank, it will, on behalf of the Issuer, have the right to suspend payment of Distributions in respect of such Investor's Preferred Securities. Investors in the Preferred Securities are required to provide written notice to the

General Partner on behalf of the Issuer if at any time any such holder of Preferred Securities owns, directly or indirectly, 10% or more of the ordinary shares of the Bank.

The distribution of this document and the offering of the Preferred Securities in certain jurisdictions may be restricted by law. Persons into whose possession this document comes are required by the General Partner, the Issuer, the Bank and the Managers to inform themselves about, and to observe, any such restrictions. In particular, there are restrictions on the distribution of this Offering Circular and the offer and sale of the Preferred Securities, in the United States and the United Kingdom. See "Subscription and Sale".

No action has been taken to permit a public offering of the Preferred Securities in any jurisdiction where action would be required for such purpose. Accordingly, the Preferred Securities may not be offered or sold, directly or indirectly, and this Offering Circular may not be distributed in any jurisdiction, except in accordance with the legal requirements applicable in that jurisdiction. In particular, the Preferred Securities have not been, and will not be, registered under the Securities Act and are subject to United States tax law requirements. Subject to certain exceptions, the Preferred Securities may not be offered, sold or delivered within the United States or to US persons. A further description of certain restrictions of the offering and sale of the Preferred Securities and on the distribution of this document is given under "Subscription and Sale".

The Jersey Financial Services Commission has given and has not withdrawn its consent under Article 8 of the Control of Borrowing (Jersey) Order 1958 to the creation by the Issuer of the Preferred Securities. The Jersey Financial Services Commission is protected by the Borrowing (Control) (Jersey) Law 1947, as amended, against liability arising from the discharge of its functions under that Law.

Nothing in this Offering Circular or anything communicated to Holders of, or investors in, the Preferred Securities (or any such potential Holders or investors) by the General Partner is intended to constitute or should be construed as advice on the merits of the purchase of, or subscription for, the Preferred Securities or the exercise of any rights attached thereto for the purposes of the Financial Services (Jersey) Law 1998, as amended.

An investment in the Preferred Securities is only suitable for financially sophisticated investors who are capable of evaluating the merits and risks of such investment and who have sufficient resources to be able to bear any losses which may result from such an investment.

This document is for distribution only to persons who (i) are outside the United Kingdom, (ii) investment professionals falling within article 14(5) of the Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001 (the "Promotion of Collective Investment Schemes Order") and article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2001 (the "Financial Promotion Order") who have professional experience of participating in unregulated schemes and of matters relating to investments and (iii) persons falling within article 22(2) of the Promotion of Collective Investment Schemes Order and article 49(2) of the Financial Promotion Order (all such persons together being referred to as "relevant persons"). This document is directed only at relevant persons and must not be acted on or relied on by persons who are not relevant persons. Any investment or investment activity to which this document relates is available only to relevant persons and will be engaged in only with relevant persons.

The Managers are acting for HSBC Bank Capital Funding (Sterling 1) L.P. in connection with the issue of the Preferred Securities and no-one else and will not be responsible to any person other than HSBC Bank Capital Funding (Sterling 1) L.P. for providing the protections afforded to clients of the Managers, nor for providing advice in relation to the issue of the Preferred Securities. HSBC Bank plc can be contacted at 4th Floor, 8 Canada Square, London E14 5HQ.

FORWARD-LOOKING STATEMENTS

This Offering Circular and the documents incorporated by reference herein contain various forward-looking statements regarding events and trends that are subject to risks and uncertainties that could cause the actual results and financial position of the Bank or the Bank Group to differ materially from the information presented herein or from the documents incorporated by reference herein. When used in this Offering Circular or in the documents incorporated by reference herein, the words "estimate", "project", "intend", "anticipate", "believe", "expect", "should" and similar expressions, as they are related to the Bank Group and its management, are intended to identify such forward-looking statements. You should not place undue reliance on these forward-looking statements, which speak only as of the date hereof. The Bank Group does not undertake any obligation to publicly release the result of any revisions to these forward-looking statements to reflect any events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

PRESENTATION OF FINANCIAL INFORMATION

In this Offering Circular, references to "€" and "euro" are to the single currency introduced at the start of the Third Stage of the European Economic and Monetary Union pursuant to the Treaty establishing the European Community, as amended, reference to "£", "sterling" and "pounds sterling" are to the lawful currency of the United Kingdom and references to "US$" and "US dollars" are to the lawful currency of the United States.

IN CONNECTION WITH THE OFFERING, HSBC BANK PLC IN ITS CAPACITY AS LEAD MANAGER, (THE "STABILISING MANAGER") (OR ANY PERSON ACTING FOR IT) MAY OVER-ALLOT OR EFFECT TRANSACTIONS WITH A VIEW TO SUPPORTING THE MARKET PRICE OF THE PREFERRED SECURITIES AT A LEVEL HIGHER THAN THAT WHICH MIGHT OTHERWISE PREVAIL FOR A LIMITED PERIOD. HOWEVER, THERE MAY BE NO OBLIGATION ON HSBC BANK PLC OR ANY AGENT OF IT TO DO THIS. SUCH STABILISING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME AND MUST BE BROUGHT TO AN END AFTER A LIMITED PERIOD. SUCH STABILISING SHALL BE IN COMPLIANCE WITH ALL APPLICABLE LAWS, REGULATIONS AND RULES.

AVAILABLE INFORMATION

Any statement contained herein or in a document incorporated herein shall be deemed to be modified or superseded for the purposes of this Offering Circular to the extent that a statement contained herein or in any other subsequently filed document which also is or is deemed to be incorporated by reference herein modifies or supersedes such statement. Any such statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this Offering Circular and to be a part hereof from the date of filing of such document.

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SUMMARY OF THE OFFERING

The following is qualified in its entirety, including defined terms, by the more detailed information included elsewhere in this Offering Circular.

Issuer	HSBC Bank Capital Funding (Sterling 1) L.P., a limited partnership established in Jersey and registered under the Limited Partnerships (Jersey) Law, 1994 (the "**Law**"). The Issuer will be consolidated in the group accounts of HSBC Bank plc (the "Bank"). The general partner of the Issuer is HSBC Bank (General Partner) Limited (the "General Partner"), a wholly owned Jersey incorporated subsidiary of the Bank.
Guarantor	HSBC Bank plc.
Issue Details	£700,000,000 5.844% Non-cumulative Step-up Perpetual Preferred Securities, each with a nominal amount of £1,000, constituting limited partnership interests in the Issuer (the "Preferred Securities"). The Bank will guarantee, on a subordinated basis, all payments in respect of the Preferred Securities. The Preferred Securities, together with the Guarantee, are intended to provide investors with rights to income and capital distributions and distributions upon liquidation of the Bank that are equivalent to the rights they would have had if they had purchased non-cumulative perpetual preference shares of the Bank. The total nominal amount of the Preferred Securities will at issue be included in the Tier 1 capital of the Bank. Neither the Issuer nor any member of the Bank Group will make or procure any payment to investors if such a payment could not lawfully have been made had investors held shares ranking *pari passu* with Substitute Preference Shares of the Bank instead of the Preferred Securities.
Income Distributions	Non-cumulative distributions (the "Distributions") will accrue on the nominal amount of the Preferred Securities (i) from (and including) 5 November 2003 (the "Issue Date") to (but excluding) the First Optional Redemption Date (as defined below) at a fixed rate per annum of 5.844% payable annually in arrear, and (ii) from and (including) the First Optional Redemption Date for each successive six month period thereafter at a floating rate per annum equal to the sum of 1.76% and six-month LIBOR (as defined below) for such period payable semi-annually in arrear subject in each case to "*Limitations on Payment*" below. See "*Description of the Preferred Securities – Distributions*".
Distribution Dates	Distributions will, if payable, be paid on 5 November in each year beginning on 5 November 2004, the first such Distribution being calculated in respect of the period from (and including) 5 November 2003 to (but excluding) 5 November 2004. The date on which a Distribution will, if payable, be paid is referred to as a "Distribution Date". The period from (and including) the Issue Date to (but excluding) the first Distribution Date and each period

	from (and including) a Distribution Date to (but excluding) the next succeeding Distribution Date is referred to as a "Distribution Period".
Limitations on Payment.	The Issuer will pay Distributions out of, and to the extent of, its legally available resources. Distributions will not be paid on the Preferred Securities in respect of any Distribution Period on the next following Distribution Date to the extent that (i) on the relevant Distribution Date the Bank (a) is prevented by applicable UK banking regulations or other requirements from making payment in full (A) of dividends or other distributions on its Parity Obligations (as defined below) or (B) under the Guarantee or (b) is unable to make such payment of dividends or other distributions on its Parity Obligations or under the Guarantee without causing a breach of the FSA's capital adequacy requirements from time to time applicable to the Bank; or (ii) the amount of such Distribution (if paid in full), together with the sum of any dividends and other distributions on the Bank's Parity Obligations due and payable on that Distribution Date or under the Guarantee, would exceed the Adjusted Distributable Reserves (as defined below) of the Bank. No payment will be made by, or may be claimed from, the Bank in respect of a Distribution to the extent that it is not paid by reason of the limitations described above. See "*Description of the Preferred Securities – Distributions*".
Dividend Stopper.	The Bank has covenanted under the Guarantee that, if for any single Distribution Period ending on or before the First Optional Redemption Date or thereafter for any two consecutive Distribution Periods, Distributions have not been made in full, by reason of the limitations on payment described above, it will not pay dividends or other distributions in respect of its ordinary shares or effect any repurchase or redemption in respect of its ordinary shares or any other Bank securities or obligations ranking junior to the Guarantee or repurchase or redeem any Parity Obligations which are securities until after the next following Distribution Date on which a Distribution in respect of the Preferred Securities is paid in full.
Maturity	The Preferred Securities are perpetual securities and have no maturity date. The Preferred Securities may be redeemed at the option of the General Partner in the circumstances described under "*Optional Redemption*", "*Tax Call*" and "*Regulatory Call*" below.
Optional Redemption.	The Preferred Securities are redeemable, in whole but not in part and subject to paragraph 7.3 of "*Description of the Preferred Securities*", the Law and the limitations on redemption described below, at the option of the General Partner on 5 November 2031 (the "First Optional Redemption Date") or on each Distribution Date thereafter at the Optional Redemption Price. The Optional Redemption Price of each of the Preferred Securities is an amount equal to its nominal amount.

	See "*Description of the Preferred Securities – Redemption and Purchase*".
Tax Call.	The Preferred Securities are redeemable, in whole but not in part and subject to paragraph 7.3 of "*Description of the Preferred Securities*", the Law and the limitations on redemption described below, at the option of the General Partner at any time that a Tax Event has occurred and is continuing, at the Tax Redemption Price.
Tax Redemption Price	The "Tax Redemption Price" of each of the Preferred Securities is an amount equal to its nominal amount together with any accrued but unpaid Distribution in respect of the Distribution Period (as defined above) in which the redemption date falls. See "*Description of the Preferred Securities – Redemption and Purchase*".
Tax Event	"Tax Event" means: (1) that, as a result of a change in any law or regulation of the United Kingdom or Jersey, or in any treaty to which the United Kingdom or Jersey is a party, or in the official interpretation or application of any law, regulation or treaty by any relevant body in Jersey or the United Kingdom or any action taken by any appropriate authority there is more than an insubstantial risk that (i) the Issuer or the General Partner would be subject to more than a *de minimis* amount of tax (except, in the case of the General Partner only, for any such tax that would arise as a result of (a) profits arising to it as a result of payments received by it from the Issuer or (b) activities (if any) carried on by it other than those permitted or contemplated in the Partnership Agreement (as defined under "HSBC Bank Capital Funding (Sterling 1) L.P.") in Jersey or the United Kingdom, (ii) payments to holders would be subject to deduction or withholding for or on account of tax or would give rise to any obligation to account for any tax in Jersey or the United Kingdom, (iii) payments by the Bank in respect of the Subordinated Note (as defined below) would be subject to deduction or withholding for or on account of tax in the United Kingdom or (iv) the Bank would not obtain relief for the purposes of UK corporation tax for any payment of interest in respect of the Subordinated Note; or (2) that there is more than an insubstantial risk that any of the events described in paragraphs (i) to (iv) above may occur other than as a result of a change in any law or regulation of the United Kingdom or Jersey, or in any treaty to which the United Kingdom or Jersey is a party, or in the official interpretation or application of any law, regulation or treaty by any relevant body in Jersey or the United Kingdom or any action taken by any appropriate authority.

Regulatory Call.	The Preferred Securities are redeemable, in whole but not in part and subject to paragraph 7.3 of "*Description of the Preferred Securities*", the Law and the limitations on redemption described below, at the option of the General Partner at any time a Regulatory Event (as defined below) has occurred and is continuing, at the Regulatory Event Redemption Price. The "Regulatory Event Redemption Price" of each of the Preferred Securities is an amount equal to, in the case of a redemption on a date which is prior to the First Optional Redemption Date, the higher of (i) its nominal amount together with any accrued but unpaid Distribution in respect of the Distribution Period in which the redemption date falls and (ii) the Make Whole Amount (as defined below) and, in the case of a redemption on or after the First Optional Redemption Date, its nominal amount together with any accrued but unpaid Distribution in respect of the Distribution Period in which the relevant redemption date falls. See "*Description of the Preferred Securities – Redemption and Purchase*".
Regulatory Event	"Regulatory Event" means that for any reason, there is more than an insubstantial risk that for the purposes of the FSA's capital adequacy requirements applicable to banks in the United Kingdom at that time the total nominal amount of the Preferred Securities may not be included in the Tier 1 capital of the Bank on both a solo basis and on a consolidated basis.
Substitution after a Regulatory Event or a Tax Event	If a Regulatory Event or a Tax Event has occurred and is continuing, as an alternative to redemption and at the option of the General Partner, the Substitute Preference Shares (as defined below) may (provided that proceedings have not been commenced for the liquidation, dissolution or winding up of the Bank in England) be substituted for the Preferred Securities as if the Regulatory Event or the Tax Event constituted a Substitution Event.
Limitations on Redemption . . .	The Preferred Securities may only be redeemed if (i) the aggregate of the Bank's Adjusted Distributable Reserves and the proceeds of any issue of Replacement Capital (as defined below) made for the purpose of funding such redemption is at least equal to the full amount payable on redemption, and (ii) the prior consent of the FSA, if required, has been obtained.
Make Whole Amount.	In respect of a Preferred Security, "Make Whole Amount" means at any time prior to the First Optional Redemption Date an amount equal to the sum of (i) the present value of its nominal amount; and (ii) the present value of each remaining scheduled Distribution to and including the First Optional Redemption Date, discounted from the First Optional Redemption Date or the relevant Distribution Date, respectively, in each case to the Early Redemption Date at a rate equal to the sum of (x) 0.375% and (y) the Reference Rate (as defined below).

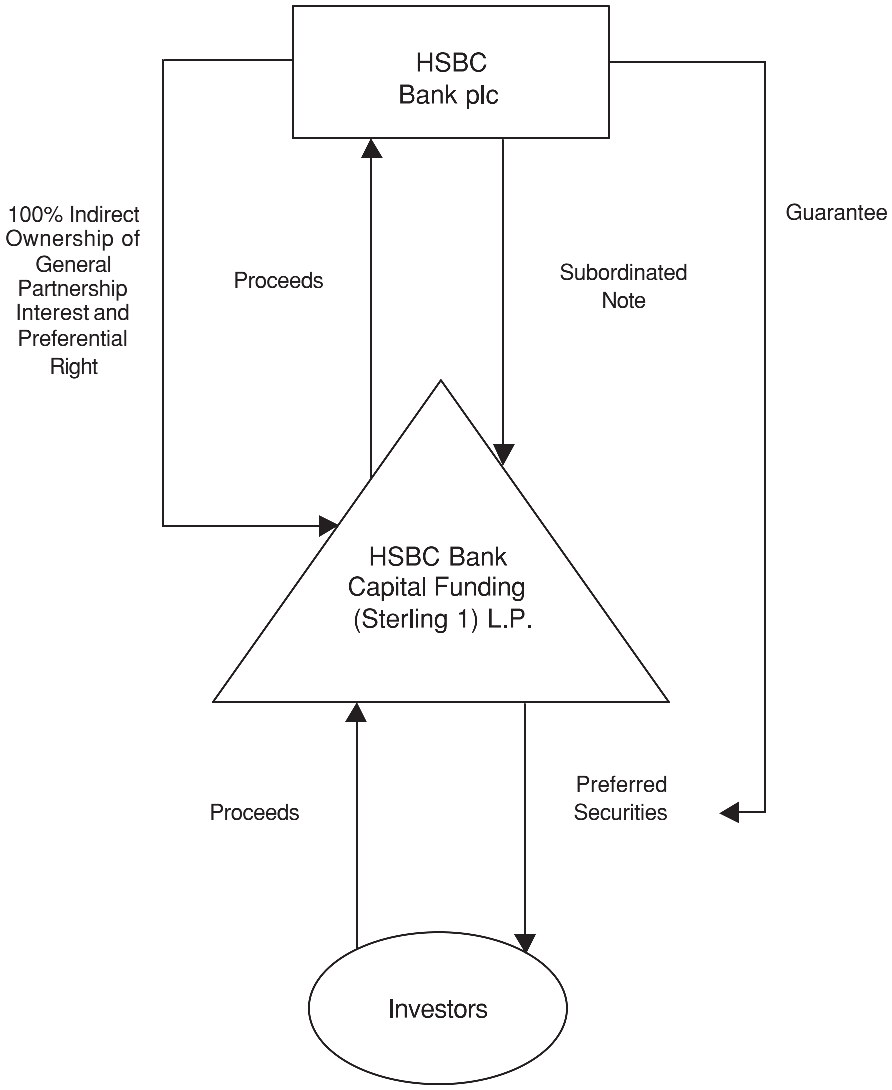
Substitution Event	A Substitution Event will occur if: (i) on the Distribution Date in November 2048 the Preferred Securities (or any of them) are outstanding and no notice has been given to redeem the then outstanding Preferred Securities on or before the Distribution Date in November 2048; (ii) the Bank's total capital ratio, calculated on a solo basis and consolidated basis in accordance with applicable UK bank capital adequacy regulations, falls below the then minimum ratio required by such regulations; or (iii) the Bank's board of directors in its sole discretion has notified the FSA and the Issuer that it has determined that (ii) above is expected to occur in the near term. Upon the occurrence of a Substitution Event and provided that proceedings have not been commenced for the liquidation, dissolution or winding up of the Bank in England, the Preferred Securities will, as soon as reasonably practicable thereafter, be substituted by the Substitute Preference Shares. See "*Description of the Preferred Securities – Substitution by Substitute Preference Shares*".
Substitute Preference Shares . . .	The Substitute Preference Shares will be fully-paid non-cumulative redeemable perpetual preferred shares issued by the Bank having economic terms which are in all material respects equivalent to those of the Preferred Securities and the Guarantee taken together. The Bank will take all reasonable steps to procure that the Substitute Preference Shares will at the relevant time be admitted to listing on the Official List of the Financial Services Authority (in its capacity as competent authority for the purposes of Part IV of the Financial Services and Markets Act 2000 (the "FSMA")) (the "UK Listing Authority") and to trading on the London Stock Exchange plc (the "London Stock Exchange") or another Recognised Stock Exchange (as defined herein).
Rights upon Liquidation.	In the event of the dissolution or winding up of the Issuer, each investor will, subject to certain limitations, be entitled to receive out of the assets of the Issuer available for distribution the Liquidating Distribution. The Liquidating Distribution will be made (i) before any distribution of assets is made to the General Partner or HSBC Preferential LP (UK) as holder of the Preferential Right and (ii) *pari passu* with equivalent claims under all outstanding Parity Obligations of the Issuer which in turn rank *pari passu* with the Liquidating Distribution but (iii) after the claims of all other creditors of the Issuer, and holders of obligations of the Issuer, whose claims are not *pari passu* with or subordinated to the Preferred Securities. "Preferential Right" means the preferential limited partnership interest in the Issuer initially held by HSBC Preferential LP (UK) and entitling it to receive in preference to the rights of the General Partner all

	amounts received by the Issuer in excess of those required to make payments of any Distribution (and, if relevant, Additional Amounts) on any Distribution Date or any Liquidating Distribution or relevant portion thereof (and, if relevant, Additional Amounts) to Holders. See "*Description of the Preferred Securities – Liquidating Distributions*".
Withholding Tax and Gross Up . .	Except in certain limited cases and subject to the limitations on payments described above, the Issuer or the Bank pursuant to the Guarantee, will pay such additional amounts ("Additional Amounts") as may be necessary in order that the net payments in respect of the Preferred Securities, after withholding for any taxes imposed by Jersey or the United Kingdom, as the case may be, on such payments will equal the amount which would have been received in the absence of any such withholding.
Certain Restrictions	Other than the Issuer's ordinary expenses, which will be borne by the Bank and/or the General Partner, and except for fees and commissions payable in connection with the issue of the Preferred Securities, the General Partner has covenanted not to incur any indebtedness in the name of the Issuer or other obligations ranking, in respect of distributions or other payments, senior to the rights of holders.
Parity Obligations	"Parity Obligations" means (i) in relation to the Bank, any preference shares or other obligations of the Bank that constitute Tier 1 capital of the Bank on a consolidated basis and do not rank in all material respects senior or junior to the Bank's obligations under the Guarantee and any other guarantee or support agreement given by the Bank in respect of any preference shares, or other preferred securities (not constituting debt obligations) having in all material respects the same ranking as preference shares, issued by any subsidiary undertaking of the Bank that constitutes Tier 1 capital of the Bank on a consolidated basis and does not rank in all material respects senior or junior to the Guarantee and (ii) in relation to the Issuer, any preferred securities (other than the Preferred Securities) issued by it or other obligations of it which are entitled to the benefit of the Guarantee or any guarantee of the Bank ranking *pari passu* with the Guarantee.
Guarantee	The Bank will guarantee, on a subordinated basis, all payments in respect of the Preferred Securities. The Guarantee constitutes unsecured obligations of the Bank which will, in the event of the winding up of the Bank, be subordinated in right of payment to the claims of all other creditors of the Bank (including certain subordinated creditors) other than creditors whose claims rank or are expressed to rank *pari passu* with or junior to the Guarantee or other obligations of the Bank ranking *pari passu* with or junior to the Guarantee. The Bank will not be obliged to make a payment under the Guarantee (i) unless it is able to make such payment and be Solvent (as defined in the Guarantee)

	immediately thereafter and (ii) if such payment would cause it to be in breach of applicable banking regulations or capital adequacy requirements. See "*Description of the Guarantee*".
Subordinated Note	Payments in respect of the Preferred Securities will be funded by payments received by the Issuer under the £700,000,000 5.844% Fixed/Floating Rate Subordinated Note in bearer form issued by the Bank on the Issue Date (the "Subordinated Note"). The Subordinated Note will have economic terms which are in all material respects equivalent terms to those of the Preferred Securities, save that (i) the interest payable on the Subordinated Note will be cumulative and (ii) the Subordinated Note will be due on 30 November 2048. In the event that the Subordinated Note or any Replacement Debt is redeemed while any Preferred Securities remain outstanding and are not subject to a notice of redemption, the General Partner has undertaken to invest the proceeds of redemption of the Subordinated Note or any Replacement Debt in a subordinated note of the Bank with a maturity date of 5 November 2048 and economic terms essentially equivalent to the Subordinated Note (including that the interest rate will reflect the then current Distribution Rate provisions of the Preferred Securities). Interests in the Subordinated Note will not be delivered or otherwise made available in any form to holders of the Preferred Securities, and the rights of such holders shall be represented solely by Preferred Securities in registered form.
Voting Rights	Except as stated below and provided for in the Law, holders of Preferred Securities will not be entitled to receive notice of, attend or vote at any meeting of partners of the Issuer or participate in the management of the Issuer. If for any Distribution Period ending on or before the First Optional Redemption Date or thereafter for any two consecutive Distribution Periods Distributions have not been paid in full (and/or the Bank has not made the required payments under the Guarantee in respect of such Distribution), holders will be entitled by written notice to the Issuer given by the holders of a majority in nominal amount of the Preferred Securities or by a resolution passed at an appropriately constituted meeting to appoint a special representative to enforce their statutory rights, including provision of information on the affairs of the Issuer. Such special representative must vacate its office if, after its appointment, a full Distribution is made by the Issuer, or by the Bank under the Guarantee, for a full Distribution Period, or an amount equivalent to the Distribution to be paid in respect of a full Distribution Period has been paid or irrevocably set aside in a separately designated trust account for payment to holders.
Variation of Rights.	Any variation of the rights of holders (except where such variation is solely of a formal, minor or technical nature

	in which case it may be approved by the General Partner without the consent of holders) will take effect only if approved in writing by at least one-third of holders or if approved by a resolution passed by three-quarters of those present in person or by proxy at a meeting of holders at which the quorum shall be one-third by nominal amount of the holders.
Form of the Securities	The Preferred Securities will be issued in registered form. The Preferred Securities will be sold to non-US persons outside the United States pursuant to Regulation S and will, on issue, be evidenced by a Global Certificate. The Global Certificate will be registered in the name of a nominee of, and deposited with a common depositary for, Euroclear and Clearstream, Luxembourg. For so long as the Preferred Securities are deposited and registered as described above, book-entry interests in the Preferred Securities will be shown on, and transfers thereof will be effected only through, records maintained by Euroclear and Clearstream, Luxembourg. Definitive certificates evidencing Preferred Securities will be issued only in limited circumstances. See "*Description of the Preferred Securities – Transfers and Form*".
Rating	The Preferred Securities are expected to be assigned on issue a rating of A by Standard & Poor's Ratings Services, a Division of The McGraw Hill Companies, Inc., A1 by Moody's Investors Service Limited and AA- by Fitch Ratings Limited. A credit rating is not a recommendation to buy, sell or hold securities and may be subject to revision, suspension or withdrawal at any time by the relevant rating organisation.
Governing Law	The Guarantee and the Subordinated Note will be governed by English law. The Partnership Agreement and the Preferred Securities will be governed by Jersey law.
Listing	Application has been made for the Preferred Securities to be listed on the Luxembourg Stock Exchange.
Global Certificate	ISIN: XS0179407910 Common Code: 017940791

Transaction Structure



USE OF PROCEEDS

The gross proceeds from the issue of the Preferred Securities, which are expected to amount to £700,000,000, will be used by the Issuer to subscribe for the Subordinated Note. The Bank will use the gross proceeds from the issue of the Subordinated Note for general corporate purposes and for augmenting the capital base of the Bank. The Managers will receive fees and commissions as set out under "*Subscription and Sale*". The proceeds net of the fees and commissions to be paid to the Managers as set out under "*Subscription and Sale*" would amount to £693,000,000

INVESTMENT CONSIDERATIONS

Prospective investors should consider carefully the following information in conjunction with the other information contained in this Offering Circular before purchasing any Preferred Securities.

Distributions on the Preferred Securities are not cumulative.

Distributions on the Preferred Securities are not cumulative. As set out in "*Description of the Preferred Securities – Distributions*", Distributions will be paid on each Distribution Date out of interest received by the Issuer under the Subordinated Note. Distributions may not be paid in full, or at all, if the Bank does not have sufficient distributable profits or if the Bank is limited in making payments on other obligations, including the Guarantee. If Distributions for any Distribution Period are not paid by reason of the above limitations, investors will not be entitled to receive such Distributions (or any Guaranteed Payment in respect of such Distributions) whether or not funds are or subsequently become available.

The Preferred Securities have no fixed redemption date and investors have no rights to call for redemption of the Preferred Securities.

The Preferred Securities have no fixed final redemption date and holders have no rights to call for the redemption of the Preferred Securities. Although the Preferred Securities may be redeemed in certain circumstances (including at the option of the General Partner on 5 November 2031 or following the occurrence of a Tax Event or a Regulatory Event), there are limitations on redemption of the Preferred Securities, including satisfaction of the Redemption Conditions (as described herein) relating to FSA consent and the availability of sufficient funds to effect redemption.

Any Preferred Securities outstanding on the Distribution Date in November 2048 will be substituted by Substitute Preference Shares

If any Preferred Securities are outstanding on the Distribution Date in November 2048 and no notice has been given to redeem such Preferred Securities on or before the Distribution Date in November 2048, such Preferred Securities will be substituted by the Substitute Preference Shares.

The Bank's obligations under the Guarantee are limited to the amounts of the payments due under the Preferred Securities.

The ability of the Issuer to make payments on the Preferred Securities is dependent upon the Bank making the related payments on the Subordinated Note when due. If the Bank defaults on its obligations to make payments on the Subordinated Note, the Issuer will not have sufficient funds to make payments on the Preferred Securities. In those circumstances, investors will have to rely upon the Guarantee from the Bank for payment of these amounts.

The Bank's obligation to make payments under the Guarantee is limited to the extent of the amounts due under the Preferred Securities. Distributions will not be paid under the Preferred Securities if the Bank does not have available sufficient distributable profits to make payments in full on the Guarantee and all securities ranking equally to the Guarantee as to rights to dividends. Even if it has sufficient distributable profits, distributions will not be paid under the Preferred Securities if, on the date of such payment the Bank is prevented by applicable UK banking regulations or other requirements from making payment in full under the Guarantee or of any dividends or other distributions on its obligations that rank equally to the Guarantee or the Bank is unable to make such payment of dividends or other distributions without causing a breach of the capital adequacy requirements applicable to the Bank Group.

Investors will have no right to seek payment of amounts under the Guarantee that would exceed the amount investors would have been able to receive had investors been investors in directly issued non-cumulative, non-voting preference shares of the Bank.

Under no circumstances does the Guarantee provide for acceleration of any payments on, or repayment of, the Preferred Securities.

The Bank is not required to pay investors under the Guarantee unless it first makes other required payments.

The Bank's obligations under the Guarantee will rank junior to all of its liabilities to creditors and claims of holders of senior ranking securities. In the event of the winding-up, liquidation or dissolution of the Bank, its assets would be available to pay obligations under the Guarantee only after the Bank has made all payments on such liabilities and claims. None of the Preferred Securities, the Subordinated Note or the Guarantee limit the ability of the Bank and its affiliates (other than as described in "*Summary of the Offering – Certain Restrictions*") to incur additional indebtedness, including indebtedness that ranks senior in priority of payment to the Guarantee.

Non-payment of distributions may adversely affect the trading price of the Preferred Securities.

If in the future, payments are limited on the Preferred Securities because the Bank has insufficient distributable profits, the Preferred Securities may trade at a lower price. If investors sell the Preferred Securities during such a period, investors may not receive the same price as someone else who does not sell its Preferred Securities until sufficient distributable profits are available to resume distribution payments. In addition, because the Bank's obligation to make payments under the Guarantee is limited to the extent of the underlying payment obligations on the Preferred Securities which may be limited due to insufficient distributable profits, the market price for the Preferred Securities may be more volatile than other securities that do not reflect these limitations.

Investors should not rely on distributions from the Preferred Securities – they may be redeemed at any time if certain adverse consequences occur as a result of the application of UK or Jersey tax law or regulations or on the occurrence of a regulatory event in the UK and certain conditions are satisfied.

If certain consequences occur, which are more fully described below in this Offering Circular, as a result of the application of UK or Jersey tax law or regulations or on the occurrence of a regulatory event in the UK and certain other conditions which are more fully described below are satisfied, the Preferred Securities could be redeemed by the Issuer.

There can be no assurance as to the market prices for the Preferred Securities or the Substitute Preference Shares; therefore, investors may suffer a loss.

The Bank cannot give investors any assurance as to the market prices for the Preferred Securities or, following a Substitution Event, Substitute Preference Shares that may be distributed in exchange for the Preferred Securities. Accordingly, the Preferred Securities and Substitute Preference Shares may trade at a discount to the price at which investors purchased the Preferred Securities. In addition, because the Bank's obligation to make payments under the Guarantee is limited to the extent of the underlying payment obligations on the Preferred Securities which may in turn be limited due to insufficient distributable profits, the market price for these securities may be more volatile than other securities that do not reflect these limitations.

HSBC BANK CAPITAL FUNDING (STERLING 1) L.P.

Introduction

HSBC Bank Capital Funding (Sterling 1) L.P. was registered in Jersey on 31 October 2003 under the Limited Partnerships (Jersey) Law, 1994 for an unlimited duration, with HSBC Bank (General Partner) Limited as the general partner (the "General Partner"). The General Partner, HSBC Issuer Services Common Depositary Nominee (UK) Limited (the "Initial Partner"), HSBC Preferential LP (UK) (the "Preferential Limited Partner") and the Bank have entered into a partnership agreement dated the date hereof (the "Partnership Agreement") for the purpose of establishing the Issuer on 31 October 2003. The Issuer is not a legal entity separate from its partners. The Partnership Agreement is not intended to create a trust relationship between any of the partners. The Preferred Security limited partnership interests are held on the investors' behalf in the name of HSBC Issuer Services Common Depositary Nominee (UK) Limited.

Control of the Issuer

The General Partner, a wholly owned subsidiary of, and controlled by, the Bank, is the sole general partner in the Issuer and, as such, controls the Issuer.

Provided that limited partners do not become involved with the management of the Issuer other than in the circumstances provided for in the Partnership Agreement (see "*Description of the Preferred Securities – Voting Rights*"), and in accordance with applicable law the liability of the limited partners to contribute to the debts or obligations of the Issuer will be limited to the amount which they have contributed or agreed to contribute to the partnership, being £1,000 per Preferred Security.

Sole Activity

The Issuer was established for the sole purpose of raising finance for the Bank. It has carried out no operations since its registration other than in relation to the creation of the Preferred Securities. The capital contributions to be made by the limited partners will be used by the Issuer to subscribe for the Subordinated Note and pay fees and commissions as disclosed in this Offering Circular.

Management

The Issuer will be operated by the General Partner and its duly appointed delegates. The registered office of the Issuer and of the General Partner is 1 Grenville Street, St Helier, Jersey JE4 8UB. Except as provided for in the Law and as described in paragraph 8 of the section entitled "Description of the Preferred Securities", no Holder of a Preferred Security may participate in the management of the Issuer. The Bank has undertaken in the Guarantee to ensure that the General Partner will at all times be a directly or indirectly owned subsidiary of the Bank.

The General Partner has agreed in the Partnership Agreement to contribute capital from time to time to the extent necessary to pay all costs, expenses, debts, liabilities and obligations incurred in the proper maintenance and business of the Issuer (other than in respect of payments on the Preferred Securities or the Preferential Right). The General Partner has also agreed that it will at all times maintain sole ownership of its general partnership interest in the Issuer subject to the terms of the Partnership Agreement. The Partnership Agreement provides that all of the Issuer's operations will be conducted by the General Partner and the General Partner will have unlimited liability for the repayment, satisfaction and discharge of all debts and obligations of the Issuer to persons other than partners in accordance with the Limited Partnerships (Jersey) Law, 1994. Neither the Issuer nor the General Partner shall be liable to make any payment to any limited partner in respect of the Preferred Securities or the Preferential Right other than out of partnership assets.

If the Issuer is dissolved or wound up, the Partnership Agreement provides that the General Partner will only be entitled to any assets of the Issuer remaining after (i) all debts and other liabilities of the Issuer have been satisfied in full and (ii) the full Liquidating Distribution to which the holders are entitled having regard to the limitations set out herein has been paid to or irrevocably set aside for the holders and any amount payable in respect of the Preferential Right has been paid.

The General Partner has undertaken that, if the Subordinated Note is redeemed while the Preferred Securities remain outstanding and are not subject to a notice of redemption, it will invest the proceeds of the Subordinated Note or any Replacement Debt in a subordinated note of the Bank, with a maturity date of 30 November 2048 and economic terms essentially equivalent to the Subordinated Note (including that the interest rate will reflect the then current Distribution Rate provisions of the Preferred Securities).

Capital Contribution

Save for capital contributions to be made by the General Partner from time to time to meet certain operating expenses of the partnership, the capital commitment of £1,000 which the General Partner may call from HSBC Preferential LP (UK) as the Preferential Limited Partner, and the capital contribution of £700,000,000 to be made by the limited partners in relation to the Preferred Securities, there are intended to be no other contributions to the Issuer.

Indebtedness

Since the date of its registration, the Issuer has not had any loan capital outstanding, has not incurred any borrowings, has had no contingent liabilities except as disclosed herein, has not granted any guarantees and does not intend to have outstanding any such loan capital, incur any such borrowings, have any such contingent liabilities or grant any such guarantees. The General Partner has undertaken not to incur any indebtedness in the name of the Issuer other than the costs and expenses incidental to maintaining the Register, paying the fees and commissions for listing, registrar and paying agency charges in respect of the Preferred Securities, holding and exercising its rights under the Subordinated Note or any Replacement Debt and the maintenance of a custodian thereof and the administration of the Issuer.

DESCRIPTION OF THE GUARANTOR

The following information (except for the information under the heading "Recent Developments of the Guarantor") has been extracted from the Bank's Annual Report and Accounts for the year ended 31 December 2002.

HSBC Bank plc and its subsidiaries form a UK-based financial services group providing a wide range of banking, treasury and financial services to personal, commercial and corporate customers, mainly in the United Kingdom and continental Europe. The Bank's strategy is to build long-term relationships and reward customers through value-for-money products and high-quality service.

HSBC Bank plc (formerly Midland Bank plc) was formed in England in 1836 and subsequently registered as a limited company in 1880. In 1923, the company adopted the name of Midland Bank Limited which it held until 1982 when the name was changed to Midland Bank plc.

During the year ended 31 December 1992, Midland Bank plc became a wholly owned subsidiary undertaking of HSBC Holdings plc ("HSBC Holdings"), whose Group Head Office is at 8 Canada Square, London E14 5HQ. HSBC Bank plc adopted its current name, changing from Midland Bank plc, in the year ended 31 December 1999.

HSBC Holdings, together with its subsidiary undertakings, joint ventures and associates, is referred to as the "HSBC Group". The HSBC Group is one of the largest banking and financial services organisations in the world, with over 8,000 offices in 80 countries and territories in Europe, the Asia-Pacific region, the Americas, the Middle East and Africa. Its total assets at 31 December 2002 were £471 billion. The Bank is the HSBC Group's principal operating subsidiary undertaking in Europe.

Since 1999, the Bank has been following the HSBC Group's "Managing for Value" strategy, which focuses on the delivery of wealth management services to personal customers, aligning its corporate and investment banking businesses, and growing its commercial business. As part of the HSBC Group's key initiative to align corporate and investment banking, the activities of HSBC Investment Bank plc were transferred to the Bank in November 2002.

As at 31 December 2002, the Bank's principal subsidiary undertakings and their main geographical areas of activity were:

• CCF S.A. (formerly Crédit Commercial de France S.A.)	France
• HSBC Asset Finance (UK) Limited	United Kingdom
• HSBC Bank A.S.	Turkey
• HSBC Bank International Limited	Jersey
• HSBC Bank Malta p.l.c.	Malta
• HSBC Guyerzeller Bank AG	Switzerland
• HSBC Invoice Finance (UK) Limited	United Kingdom
• HSBC Life (UK) Limited	United Kingdom
• HSBC Rail (UK) Limited	United Kingdom
• HSBC Republic Bank (Guernsey) Limited	Guernsey
• HSBC Republic Bank (Suisse) SA	Switzerland
• HSBC Republic Bank (UK) Limited	United Kingdom
• HSBC Trinkaus & Burkhardt KGaA	Germany
• HSBC Trust Company (UK) Limited	United Kingdom

On 28 June 2002, Merrill Lynch HSBC Holdings Limited ("MLHSBC") became a 100 per cent owned subsidiary of the HSBC Group. On 1 November 2002, Merrill Lynch HSBC Limited was transferred to the Bank. MLHSBC was formed as a 50:50 joint venture between the HSBC Group and Merrill Lynch in April 2000 to provide direct investment and banking services, primarily over the internet, to "mass affluent" investors outside the United States. MLHSBC has a licence to continue to use Merrill Lynch as part of its name and for clients to have access to Merrill Lynch research for up to two and a half years from 28 June 2002.

On 1 July 2002, the Bank acquired a 73.47 per cent interest in HSBC Trinkaus & Burkhardt KGaA, as part of the HSBC Group's strategic restructuring to align its corporate and investment banking activities.

On 1 July 2002, the Bank acquired 97.82 per cent of HSBC Republic Bank (UK) Limited, as part of the HSBC Group's continued restructuring of its Private Banking activities.

On 19 September 2002, HSBC Bank A.S. in Turkey purchased 100 per cent of Benkar Tuketici Finansmani ve Kart Hizmetleri A.S. ("Benkar") a consumer finance and card services company, from Boyner Holding A.S.

On 30 November 2002, the investment banking activities of HSBC Investment Bank plc were transferred to the Bank.

The Bank's strategy centres on building long-term customer relationships by listening to customers, understanding their needs and delivering the most effective solutions. In accordance with this strategy, the Bank continues to invest in improving customer relationship management systems, creating more convenient channels, developing innovative and flexible products and building a reputation for fair pricing.

In line with the HSBC Group, the Bank commenced a communication programme in the UK during 2002, designed to give the HSBC brand a strongly differentiated image in the minds of customers, with the ultimate aim of increasing business. The results at the end of 2002 were encouraging, with a marked improvement in the level of awareness of the HSBC brand.

While the Bank continues to develop telephone and internet propositions, it remains committed to community banking and its most important delivery channel, the branch network where it has 1,633 branches, including 42 outlets in supermarkets. Experienced managers are located in local branches with authority to provide a timely, efficient and flexible service to both personal and business customers. Developments in the branch network continue to focus on creating more time for branch staff to serve customers by removing back office work to central processing sites.

The Bank has an extensive network of cash, pay-in and statement machines and provides some 3,000 Automated Teller Machines (ATMs) for use by customers. Customers also have access to over 42,000 cash machines through the UK LINK network and over 835,000 ATMs worldwide.

Global processing, through the establishment of Group Service Centres (GSCs), continues to play an important role in the HSBC Group's strategic aim of pursuing economies of scale in order to increase productivity and achieve a competitive and economic advantage. Since their introduction in 1996, the GSCs have progressively fulfilled more of the back office functions previously undertaken by the HSBC Group's principal members across the world, in the UK, the Hong Kong SAR, the UAE, the United States and Canada. The centres provide a wide range of activities for a growing number of business areas, including cards, mortgage processing, investment products and retail banking.

The Bank continues to seek synergies to maximise long-term value. Two outsourcing projects have now been completed: cash processing to Securitas Cash Management Limited and cheque and credit clearing services to Intelligent Processing Solutions Limited. The Bank works closely with its new partners to improve processes and systems for the benefit of customers, as well as increasing efficiency.

The Bank divides its activities into the following business segments: UK Personal Banking, UK Commercial Banking, UK Corporate and Institutional Banking, and UK Treasury and Capital Markets; Investment Banking; International Banking; CCF; Private Banking (formerly HSBC Republic); and HSBC Trinkaus & Burkhardt.

At the end of 2002, the Bank Group had total assets of £218.4 billion and shareholders' funds of £16.5 billion. For the year ended 31 December 2002, the Bank Group's operating profit was £2,145 million on operating income of £7,692 million. The Bank Group is a strongly capitalised banking group with a total capital ratio of 10.3 per cent and a Tier 1 capital ratio of 7.1 per cent as at 31 December 2002.

RECENT DEVELOPMENTS OF THE GUARANTOR

On 17 March 2003, the Bank sold a majority stake of 80.1 per cent in its European private equity business to its existing management team.

On 10 July 2003, the Bank signed a preliminary agreement with Banca Profilo for the sale of the Bank's private banking operations in Italy for a consideration of €10.8 million. The agreement covers the sale of the Bank's Italian private banking company, Società di Gestione del Risparmio, as well as its custodial services unit, private client funds and assets of the Bank's commercial lending unit in Italy. The authorisation of the Banca d'Italia has been received and the transaction will be completed at the end of November 2003.

On 26 September 2003, it was announced that William Dalton, Chief Executive of the Bank since 1998, is to retire in May 2004 after 24 years' service. Mr Dalton will be succeeded as Chief Executive of the Bank by Michael Geoghegan, currently HSBC Group General Manager South America, and President HSBC Bank Brasil S.A. – Banco Múltiplo. Mr Geoghegan, who joined the HSBC Group in 1973, will take up his new position in January 2004.

On 9 October 2003, the HSBC Group reached agreement to acquire substantially all of Lloyds TSB's onshore and offshore assets related to Brazil. Of these assets, the Bank will acquire certain Brazilian offshore loan assets held by Lloyds Bank Plc for an amount of US$220 million, and is taking over certain intra-group funding currently provided by Lloyds TSB for its Brazilian businesses. Completion of the acquisition is subject to final regulatory approval by the Central Bank of Brazil.

On 16 October 2003, the Bank informed its staff in the UK of its plans to continue to increase the amount of UK related work carried out in its Group Service Centres in China, India and Malaysia, with the number of equivalent staff working in the Centres expected to grow by 4,000 over the next three years. As a result of the transfer of work the Bank expects to close some Service Centres in the UK by the end of 2005.

Since 31 December 2002 there have been the following changes in the Directors of the Bank:

On 1 January 2003, D D J John was appointed Director and Chief Operating Officer. On 28 May 2003, K R Whitson and R Emerson resigned as Director and Deputy Chairman, and independent non-executive Director, respectively, and S K Green and J D Fishburn were appointed Deputy Chairman and independent non-executive Director, respectively.

CONSOLIDATED CAPITALISATION AND INDEBTEDNESS OF THE GUARANTOR

The following shows the unaudited consolidated capitalisation and indebtedness of HSBC Bank plc as at 30 June 2003:

	Authorised £m	Authorised US$m	Issued and fully paid £m
Ordinary Share Capital of HSBC Bank plc:			
Ordinary shares (of nominal value £1 each)	1,000	—	797
			Proceeds of Issue £m
Preference Share Capital of HSBC Bank plc			
Sterling preference shares (of nominal value £1 each)	150	—	—
U.S. Dollar preference shares (of nominal value US$0.01 each)	—	2	529

			Amount Outstanding £m
		Minority Interests – Non Equity	
€	1,900 m	Capital contribution	1,320
		Consolidated Loan Capital	
		Undated subordinated loan capital of HSBC Bank plc	
US$	750m	Undated Floating Rate Primary Capital Notes	454
US$	500m	Undated Floating Rate Primary Capital Notes	303
US$	300m	Undated Floating Rate Primary Capital Notes (Series 3)	181
£	150m	9.25% Step-up Undated Subordinated Notes	150
£	150m	8.625% Step-up Undated Subordinated Notes	150
			1,238
		Undated subordinated loan capital of subsidiary undertakings	
¥	10,000m	Undated Subordinated Variable Rate Medium Term Notes	50
		Other undated subordinated liabilities individually less than £50 million	52
			102
		Dated subordinated loan capital of HSBC Bank plc	
US$	400m	8.625% Subordinated Notes 2004	242
£	200m	9% Subordinated Notes 2005	200
US$	500m	7.625% Subordinated Notes 2006	303
US$	375m	Subordinated Step-up Coupon Floating Rate Notes 2009	226
US$	300m	6.95% Subordinated Notes 2011	181
€	250m	Floating Rate Subordinated Loan 2015	174
€	600m	4.25% Callable Subordinated Notes 2016	417
£	350m	Callable Subordinated Variable Coupon Notes 2017	350
£	350m	5% Callable Subordinated Notes 2023	350
£	300m	6.5% Subordinated Notes 2023	298
US$	300m	7.65% Subordinated Notes 2025	181
£	225m	6.25% Subordinated Notes 2041	223
			3,145
		Dated subordinated loan capital of subsidiary undertakings	
€	152m	Subordinated Callable Floating Rate Notes 2008	106
		Other dated subordinated liabilities individually less than £50 million	317
			423
		Total Consolidated Loan Capital	4,908

Notes:

(1) The authorised share capital of HSBC Bank plc comprises 999,999,999 ordinary shares of nominal value £1 each; 150,000,000 Sterling preference shares of nominal value £1 each; 244,000,000 U.S. Dollar preference shares of nominal value US$0.01 each; and one preferred ordinary share of nominal value £1.

(2) The issued, allotted and fully paid share capital of HSBC Bank plc comprises 796,969,095 ordinary shares of nominal value £1 each; 35,000,000 non-cumulative U.S. Dollar preference shares of nominal value US$0.01 each; and one preferred ordinary share of nominal value £1, all of which are beneficially owned by HSBC Holdings plc.

(3) The proceeds of the capital contribution referred to under Minority Interests – Non Equity were on-lent by HSBC Capital Funding 1 (UK) Limited Partnership (a subsidiary undertaking of the Bank) to the Bank's Paris branch by issue of €900 million 7.75% Non-cumulative Subordinated Notes 2040 and €1,000 million Floating Rate Subordinated Loan 2012.

(4) On 22 August 2003, HSBC Bank plc issued £500m 5.375% Subordinated Notes 2033.

(5) None of the above Consolidated Loan Capital is secured or guaranteed.

(6) As at 30 June 2003, HSBC Bank plc had other indebtedness of £228,356 million (including deposits by banks of £36,587 million, customer accounts of £146,253 million, debt securities in issue of £8,907 million and other liabilities of £36,609 million) and contingent liabilities of £15,907 million (comprising acceptances and endorsements of £724 million, guarantees and assets pledged as collateral security of £15,177 million and other contingent liabilities of £6 million). In addition, as at 30 June 2003, HSBC Bank plc had pledged assets of £16,073 million as security for liabilities of £6,022 million.

DESCRIPTION OF THE PREFERRED SECURITIES

The Preferred Securities are limited partnership interests in the Issuer. The following summary should be read in conjunction with, and is subject to the terms of, the Partnership Agreement, a copy of which is available as described under "General Information".

Description of the Preferred Securities

1. Definitions

In this Description of the Preferred Securities, except to the extent that the context otherwise requires:

"Additional Amounts" has the meaning given to that term in paragraph 6;

"Adjusted Distributable Reserves" means at any time the lawful distributable reserves of the Bank at such time less the cumulative amount since the Issue Date of all redemptions of and payments on (a) any shares or other securities or obligations of the Bank that are accounted for under then generally accepted accounting principles in the United Kingdom as shareholders' funds in the Bank's accounts and (b) all shares, securities or other obligations of an undertaking which are accounted for under then generally accepted accounting principles in the United Kingdom as minority interest capital in the Bank's consolidated accounts, and with recourse (whether by way of guarantee, support agreement or otherwise) to the Bank that are similar in material respects to the Preferred Securities and the Guarantee, taken together, whether or not Parity Obligations, except in each case for such amounts as have been either charged to the lawful distributable reserves of the Bank or funded at that time by an issue of Replacement Capital made for the purpose of funding such redemption as described in item (ii)(b) of the definition of "Redemption Conditions";

"Bank" means HSBC Bank plc;

"Bank Group" means the Bank together with its Subsidiaries;

"Business Day" means a day other than a Saturday or Sunday on which commercial banks and foreign exchange markets settle payments in pounds sterling and are open for general business in London;

"Calculation Agent" means HSBC Bank plc or any successor calculation agent appointed under the Agency Agreement to be dated 5 November 2003 between, *inter alia*, the Bank, the General Partner and HSBC Bank plc in its capacity as Calculation Agent;

"Calculation Date" means three Business Days prior to the Early Redemption Date;

"Clearstream, Luxembourg" means Clearstream Banking, société anonyme, Luxembourg;

"Day Count Fraction" means, prior to the First Optional Redemption Date, the actual number of days in the relevant period divided by 365 (or, if any portion of the relevant period falls in a leap year, the sum of (a) the actual number of days in that portion of the relevant period falling in a leap year divided by 366 and (b) the number of days in that portion of the relevant period falling in a non-leap year divided by 365) and, on or after the First Optional Redemption Date, the actual number of days in the relevant period divided by 365;

"Distributions" means the non-cumulative cash distributions on the Preferred Securities as described in paragraph 2 and "Distribution" has a corresponding meaning;

"Distribution Date" means 5 November in each year commencing 5 November 2004 and ending on the First Optional Redemption Date and thereafter 5 May and 5 November in each year;

"Distribution Determination Date" means the day five Business Days prior to a Distribution Date;

"Distribution Period" means the period from (and including) the Issue Date to (but excluding) the first Distribution Date and each period thereafter from (and including) one Distribution Date to (but excluding) the next following Distribution Date;

"Distribution Rate" means in respect of the Preferred Securities, (i) for each Distribution Period until the First Optional Redemption Date, 5.844% per annum and, (ii) for each Distribution Period thereafter, the sum of the six-month LIBOR and the Margin for such Distribution Period;

"Early Redemption Date" means any date designated for redemption of the Preferred Securities for tax or regulatory reasons as described under paragraphs 4.3 and 4.4;

"Euroclear" means Euroclear Bank, S.A./N.V. as operator of the Euroclear System or its successor;

"First Optional Redemption Date" means 5 November 2031;

"FSA" means the Financial Services Authority in the United Kingdom and shall include any successor organisation responsible for the supervision of banks in the United Kingdom;

"General Partner" means HSBC Bank (General Partner) Limited;

"Guarantee" means the subordinated guarantee in respect of the Preferred Securities to be executed by the Bank on 5 November 2003 as a deed poll;

"Guaranteed Payments" means collectively (i) all Distributions due on the Preferred Securities, (ii) any Distributions on the Preferred Securities which would have been due had the Issuer had sufficient legally available resources but only if, and to the extent that, the Issuer did not have such legally available resources solely due to a failure by the Bank to pay interest on the Subordinated Note or the Replacement Debt as and when due and payable under the terms thereof, (iii) any Liquidating Distribution, (iv) any cash amounts to which the Holders are entitled in respect of redemption of the Preferred Securities and (v) any Additional Amounts, payment of which is in each case guaranteed by the Bank under the Guarantee;

"Holder" means, in respect of each Preferred Security, each person registered on the Register as the limited partner holding such Preferred Security at the relevant time;

"Issue Date" means 5 November 2003;

"Issuer" means HSBC Bank Capital (Sterling 1) L.P. acting by the General Partner;

"Jersey" means the Island of Jersey;

"Law" means the Limited Partnerships (Jersey) Law, 1994, as amended or restated from time to time;

"Limited Partnerships Registrar" means the person appointed as Registrar of Limited Partnerships pursuant to the Law;

"Liquidating Distribution" in respect of any Preferred Security upon a dissolution or winding up of the Issuer, means the nominal amount together with any accrued but unpaid Distribution from and including the commencement of the Distribution Period in which the date of the dissolution or winding up falls (less any interim Liquidating Distribution that may have been paid);

"London Stock Exchange" means the London Stock Exchange plc;

"Make Whole Amount" in respect of a Preferred Security means, at any time prior to the First Optional Redemption Date, an amount equal to the sum of:

(i) the present value of its nominal amount; and

(ii) the present value of each remaining scheduled Distribution to and including the First Optional Redemption Date

discounted from (i) in relation to the nominal amount, the First Optional Redemption Date, and (ii) in relation to each such remaining scheduled Distribution, the relevant

Distribution Date, in each case to the Early Redemption Date at a rate equal to the sum of (x) 0.375% and (y) the Reference Rate on an annual compounding basis (rounded to four decimal places);

"Margin" means 1.76%;

"Optional Redemption Date" means the First Optional Redemption Date and each Distribution Date thereafter;

"Optional Redemption Price" in respect of a Preferred Security means an amount equal to the nominal amount;

"Parity Obligations" means (i) in relation to the Bank, any preference shares or other obligations of the Bank that constitute Tier 1 capital of the Bank on a consolidated basis and do not rank in all material respects senior or junior to the Bank's obligations under the Guarantee and any other guarantee given or support agreement entered into by the Bank in respect of any preference shares, or other preferred securities (not constituting debt obligations) having in all material respects the same ranking as preference shares, issued by any Subsidiary, that constitute Tier 1 capital of the Bank on a consolidated basis and do not rank in all material respects senior or junior to the Guarantee and (ii) in relation to the Issuer, any preferred securities (other than the Preferred Securities) issued by it or other obligations of it which are entitled to the benefit of the Guarantee or any guarantee of the Bank ranking *pari passu* with the Guarantee;

"Partnership Agreement" means the limited partnership agreement dated 31 October 2003 between the General Partner, HSBC Issuer Services Common Depositary Nominee (UK) Limited as the Initial Partner, HSBC Preferential LP (UK) as the holder of the Preferential Right and the Bank pursuant to which the Issuer was established, as the same may be amended from time to time;

"Paying Agent" means each of HSBC Republic Bank (Jersey) Limited, HSBC Bank plc and Kredietbank S.A. Luxembourgeoise or such other entity as is appointed by the General Partner on behalf of the Issuer and notified to the Holders in the manner described in paragraph 10;

"Permitted Reorganisation" means a solvent reconstruction, amalgamation, reorganisation, merger or consolidation whereby all or substantially all business, undertaking and assets of the Bank are transferred to a successor entity which assumes all the obligations under the Guarantee;

"Preferential Right" means the preferential limited partnership interest in the Issuer initially held by HSBC Preferential LP (UK) and entitling it to receive in preference to the rights of the General Partner all amounts received by the Issuer in excess of those required to make payments of any Distribution (and, if relevant, Additional Amounts) on any Distribution Date or any Liquidating Distribution or relevant proportion thereof (and, if relevant, Additional Amounts) to Holders in accordance with paragraphs 2 or 3 below;

"Preferred Capital Contribution" means, in relation to the Preferred Securities, the aggregate contribution to the assets of the Issuer (being a whole multiple of £1,000) paid in cash to or to the order of the Issuer in respect of the Preferred Securities;

"Preferred Securities" means the £700,000,000 5.844% Non-cumulative Step-up Perpetual Preferred Securities, ranking *pari passu* amongst themselves and representing the interest of a Holder in the Issuer attributable to the relevant proportion of the Preferred Capital Contribution (being a whole multiple of £1,000);

"Recognised Stock Exchange" has the meaning given to that term in section 841 of the Income and Corporation Taxes Act 1988 of the United Kingdom;

"Redemption Conditions" means (i) that the consent of the FSA to the redemption, if then required, has been obtained and (ii) that the aggregate of (a) the Adjusted Distributable Reserves of the Bank as at the date proposed for redemption and (b) the proceeds available from an issue of Replacement Capital that has been made for the purpose of funding the redemption, is at least equal to the aggregate of the full amount payable on the redemption (including any Distribution payable on redemption);

"Redemption Date" means an Early Redemption Date or an Optional Redemption Date, as applicable;

"Reference Rate" means, in respect of the Calculation Date, the gross redemption yield (as calculated by the Calculation Agent on the basis indicated by the United Kingdom Debt Management Office in the paper "Formulae for Calculating Gilt Prices from Yields" page 4, Section one Price/Yield Formulae "Conventional Gilts; Double-dated and Undated Gilts with Assumed (or Actual) Redemption on a Quasi Coupon Date" (published 8th June 1998) on a semi-annual compounding basis (rounded, if necessary, to four decimal places) of the Reference Security, with the price of the Reference Security for this purpose being the arithmetic average of the bid and offered prices of the Reference Security quoted (to four decimal places) by the Reference Rate Market Makers at 3.00 p.m. (London time) on the Calculation Date on a dealing basis for settlement on the next following Business Day;

"Reference Rate Market Makers" means three brokers of gilts and/or gilt-edged market makers chosen by the Calculation Agent for the purpose of calculating the Reference Rate;

"Reference Security" means such U.K. government gilt-edged security as has, immediately prior to the Early Redemption Date, a maturity nearest to the next Optional Redemption Date as may be selected by the Calculation Agent with the advice of the Reference Rate Market Makers;

"Register" means the register of Holders maintained outside the United Kingdom on behalf of the Issuer under the Law;

"Registrar" means, in relation to the Preferred Securities, HSBC Republic Bank (Jersey) Limited or such other entity appointed by the General Partner on behalf of the Issuer having its office outside the United Kingdom and notified to the Holders in the manner described in paragraph 10;

"Regulatory Event" means that for any reason there is more than an insubstantial risk that for the purposes of the FSA's capital adequacy requirements applicable to banks in the United Kingdom at that time the Preferred Securities may not be included in the Tier 1 capital of the Bank on both a solo basis and a consolidated basis;

"Regulatory Event Redemption Price" means, in relation to a redemption of a Preferred Security prior to the First Optional Redemption Date, an amount equal to the higher of (i) its nominal amount (together with any accrued but unpaid Distribution in respect of the Distribution Period in which the relevant redemption falls) and (ii) the Make Whole Amount and, in relation to any other redemption of a Preferred Security, means its nominal amount (together with any accrued but unpaid Distribution in respect of the Distribution Period in which the relevant redemption falls);

"Relevant Proportion" means (a) in relation to any partial payment of a Distribution, the amount of Adjusted Distributable Reserves as of the Distribution Determination Date divided by the sum of (i) the total amount originally scheduled to be paid by way of Distribution on the Preferred Securities on the relevant Distribution Date and (ii) the sum of any dividends or other distributions or payments in respect of the Bank's Parity Obligations due and payable on that Distribution Date, converted where necessary into the same currency in which Adjusted Distributable Reserves are reported by the Bank; and (b) in relation to any partial payment of any Liquidating Distribution, the total amount available for any such payment and for making any Liquidating Distribution on any Parity Obligations divided by the sum of (i) the full Liquidating Distribution before any reduction or abatement hereunder and (ii) the amount (before any reduction or abatement hereunder) of the full liquidating distribution on any Parity Obligations of the Bank, converted where necessary into the same currency in which liquidation payments are made to creditors of the Bank;

"Replacement Capital" means shares, securities or other obligations as are mentioned in (a) or (b) in the definition of Adjusted Distributable Reserves;

"Replacement Debt" has the meaning given to that term in paragraph 9.2;

"six-month LIBOR" means:

(a) the offered rate (rounded, if necessary, up to the nearest one hundred thousandth of a percentage point (0.000005 per cent. being rounded upwards)) for six-month pounds sterling deposits as at 11.00 a.m. (London time) on the first day of the relevant Distribution Period as appears on the display designated as page "3750" on the Moneyline Telerate Service (or such other page or service as may replace it for the purpose of displaying such information) as determined by the Calculation Agent;

(b) if such offered rate does not appear, the arithmetic mean (rounded, if necessary, up to the nearest one hundred thousandth of a percentage point (0.000005 per cent. being rounded upwards)) of offered quotations to leading banks in the London interbank market for six-month pounds sterling deposits as at 11.00 a.m. (London time) on the first day of the relevant Distribution Period obtained by the Calculation Agent from the principal London offices of four major banks provided at least two of the major banks provide the Calculation Agent with such offered quotations; and

(c) if, on first day of the relevant Distribution Period to which the provisions of sub-paragraph (b) above apply, one only or none of the major banks provides the Calculation Agent which such a quotation, the arithmetic mean (rounded, if necessary, up to the nearest one hundred thousandth of a percentage point (0.000005 per cent. being rounded upwards)) of the pounds sterling lending rates which major banks in London selected by the Calculation Agent are quoting at approximately 11.00 a.m. (London time) on the first day of the relevant Distribution Period to leading banks in London for a period of six months,

except that, if the banks so selected by the Calculation Agent are not quoting as mentioned above, the six-month LIBOR shall be the six-month LIBOR in effect for the last preceding Distribution Period;

"Securities Act" means the US Securities Act of 1933, as amended;

"Special Representative" has the meaning given to that term in paragraph 8;

"Stock Exchange" means the Luxembourg Stock Exchange (or any successor organisation) or the London Stock Exchange or such other Recognised Stock Exchange approved by the General Partner on which the Preferred Securities (or any Substitute Preference Shares) may be listed from time to time;

"Subordinated Note" means the £700,000,000 5.844% Fixed/Floating Rate Subordinated Note in bearer form due on 30 November 2048 to be issued by the Bank on the Issue Date and subscribed for by the Issuer using the proceeds of the issue of the Preferred Securities;

"Subsidiary" means any entity which is for the time being a subsidiary undertaking of the Bank (within the meaning given to this term in the United Kingdom Companies Act 1989) and "Subsidiaries" has a corresponding meaning;

"Substitute Preference Shares" has the meaning given to that term in paragraph 5.1;

"Substitution Event" means that (i) on the Distribution Date in November 2048 the Preferred Securities (or any of them) are outstanding and no notice has been given to redeem the then outstanding Preferred Securities on or before the Distribution Date in November 2048 pursuant to paragraph 4; (ii) the Bank's total capital ratio, calculated on a solo basis and consolidated basis in accordance with applicable UK bank capital adequacy regulations, has fallen below the then applicable minimum ratio required by such regulations; or (iii) the Bank's board of directors in its sole discretion has notified the FSA and the Issuer that it has determined, in view of the Bank's deteriorating financial condition, that (ii) above is expected to occur in the near term;

"Substitution Event Date" means the earliest of (a) the Distribution Date in November 2048; (b) the date falling 30 days after notice is given by the Bank in accordance with paragraph 10 that Substitute Preference Shares are available for issue following a

Substitution Event falling within (ii) or (iii) of the definition of Substitution Event; or (c) the day on which a Former Holder is registered as the holder of Substitute Preference Shares;

"Tax Event" means (A) that, as a result of a change in any law or regulation of the United Kingdom or Jersey, or in any treaty to which the United Kingdom or Jersey is a party, or in the official interpretation or application of any law, regulation or treaty by any relevant body in the United Kingdom or Jersey or any action taken by any appropriate authority there is a more than insubstantial risk that (i) the Issuer or the General Partner would be subject to more than a *de minimis* amount of tax (except, in the case of the General Partner only, for any such tax that would arise as a result of (a) profits arising to it as a result of payments received by it from the Issuer or (b) activities (if any) carried on by it other than those permitted or contemplated in the Partnership Agreement) in Jersey or the United Kingdom, (ii) payments to Holders would be subject to deduction or withholding for or on account of tax or would give rise to any obligation to account for any tax in Jersey or the United Kingdom, (iii) payments by the Bank in respect of the Subordinated Note would be subject to deduction or withholding for or on account of tax in the United Kingdom, or (iv) the Bank would not obtain relief for the purposes of United Kingdom corporation tax for any payment of interest in respect of the Subordinated Note, or (B) that there is more than an insubstantial risk that any of the events listed in (i) to (iv) may occur other than as a result of a change in any law or regulation of the United Kingdom or Jersey, or in any treaty to which the United Kingdom or Jersey is a party, or in the official interpretation or application of any law, regulation or treaty by any relevant body in the United Kingdom or Jersey or any action taken by any appropriate authority;

"Tax Redemption Price" means, in respect of a redemption of a Preferred Security, the Optional Redemption Price together with any accrued but unpaid Distribution in respect of the Distribution Period in which the Preferred Security is redeemed;

"Treaty" means the Treaty establishing the European Community, as amended;

"UK" and the "United Kingdom" means the United Kingdom of Great Britain and Northern Ireland; and

"UK Listing Authority" means the Financial Services Authority in its capacity as a competent authority for the purposes of Part VI of the Financial Services and Markets Act 2000.

2. Distributions

2.1 Subject as provided by the Law and in paragraphs 2.3, 2.9 and 7.3, Distributions shall accrue from the Issue Date and shall be payable in arrear on each Distribution Date (or where any Distribution Date is not a Business Day, on the succeeding Business Day without interest in respect of such delay).

2.2 Subject to the Law, Distributions in respect of any Distribution Period will be payable at the applicable Distribution Rate on the nominal amount of the Preferred Security.

The Calculation Agent will at or as soon as practicable after each time at which the Distribution Rate is to be determined, determine the Distribution Rate for the relevant Distribution Period. Each such determination will be notified to the Issuer, the Registrar, the Stock Exchange and the Holders at the commencement of the relevant Distribution Period.

2.3 Distributions will be non-cumulative and will accrue on a day by day basis in accordance with the Day Count Fraction. Distributions will be payable out of the Issuer's own legally available resources on the relevant Distribution Date. Notwithstanding receipt of any interest due under the Subordinated Note or any other resources legally available for distribution by the Issuer, neither the Issuer nor the Bank will, save to the extent provided in paragraph 2.4, pay a Distribution or make any payment in respect of a Distribution under the Preferred Securities or the Guarantee if, on the relevant Distribution Date:

2.3.1 the Bank would be prevented by applicable UK banking regulations or other requirements from making payment in full (a) of dividends or other distributions due and payable on its Parity Obligations or (b) under the Guarantee; or

2.3.2 the amount of such Distribution (if paid in full), together with the sum of any dividends and other distributions on the Bank's Parity Obligations due and payable on that Distribution Date or under the Guarantee, would exceed the Adjusted Distributable Reserves of the Bank as of the Distribution Determination Date immediately preceding the relevant Distribution Date.

2.4 If, whether by reason of the provisions of paragraph 2.3 or any equivalent article or term of a Parity Obligation, on any Distribution Date Distributions are not paid in full on the Preferred Securities or dividends or other distributions are not paid in full on any Parity Obligations, but Adjusted Distributable Reserves are sufficient so as to allow payment of part of any Distribution, then each Holder will be entitled to receive the Relevant Proportion of any such Distribution. No Holder shall have any claim in respect of any Distribution or part thereof not payable as a result of the limitations set out in paragraph 2.3. Accordingly, such amount will not accumulate for the benefit of the Holders or entitle the Holders to any claim in respect thereof against the Issuer or the Bank under the Guarantee.

2.5 The Bank has covenanted in the Guarantee in favour of Holders that, in the event that for any single Distribution Period ending on or before the First Optional Redemption Date or thereafter for any two consecutive Distribution Periods the Distributions are not paid in full as a result of paragraph 2.3, it will not (a) declare or pay any dividends or other distributions in respect of its ordinary shares or (if permitted) effect any repurchase or redemption of its ordinary shares or any other security of the Bank ranking junior to the Guarantee (or contribute any moneys to a sinking fund for the redemption of any such shares or securities) until after the next following Distribution Date on which a Distribution in respect of the Preferred Securities is paid in full (or an amount equivalent to the Distribution to be paid in respect of the next Distribution Period has been paid or irrevocably set aside in a separately designated trust account for payment to the Holders) or (b) (if permitted) repurchase or redeem Parity Obligations which are securities until after the next following Distribution Date on which a Distribution in respect of the Preferred Securities is paid in full (or an amount equivalent to the Distribution to be paid in respect of the next Distribution Period has been paid or irrevocably set aside in a separately designated trust account for payment to the Holders).

2.6 The Bank will determine whether as of each Distribution Determination Date sufficient Adjusted Distributable Reserves exist to allow a payment of some or all of the relevant Distribution. In the event that any Distribution cannot be paid in full, the Bank will notify or procure notification to the Stock Exchange, the General Partner, the Registrar and the Paying Agent, and to Holders in accordance with paragraph 10, of the fact and of the amount, if any, to be paid in respect of that Distribution.

2.7 Save as described above, Holders will have no right to participate in the profits of the Issuer or the Bank and, in particular, will have no rights to receive from the Issuer amounts paid under the Subordinated Note in excess of Distributions due and payable under the Preferred Securities. In the event that any amounts paid in respect of the Subordinated Note exceed the amount (if any) then due by way of Distribution under the Preferred Securities, the amount of such excess will be paid to the holder of the Preferential Right and Holders will have no rights in respect thereof.

2.8 The liability of a Holder to contribute to the debts or obligations of the Issuer (if any) shall not (subject to the Law) exceed the amount of that Holder's Preferred Capital Contribution.

2.9 If at any time the General Partner becomes aware that a Holder of Preferred Securities owns, directly or indirectly, 10% or more of the ordinary shares of the Bank, the General Partner on behalf of the Issuer will have the right to suspend payment of Distributions in respect of Preferred Securities held for such holder. Holders are required to provide written notice to the General Partner on behalf of the Issuer if at any time any such investor owns, directly or indirectly, 10% or more of the ordinary shares of the Bank. Any amounts so suspended will be forfeited and may not be subsequently claimed.

3. Liquidating Distributions

3.1 In the event of the commencement of any dissolution or winding up of the Issuer before any redemption of the Preferred Securities or any substitution of the Preferred Securities by Substitute Preference Shares under paragraph 5, the Holders at that time will be entitled to receive the Liquidating Distribution, in respect of each Preferred Security held, out of the assets of the Issuer available for distribution to such Holders under the Law. Such entitlement will arise (i) before any distribution of assets is made to the General Partner or to the holder of the Preferential Right and (ii) *pari passu* with the equivalent claims under all outstanding Parity Obligations of the Issuer but (iii) after the claims of all other creditors of the Issuer and holders of obligations of the Issuer which are not Parity Obligations nor subordinated to the Preferred Securities.

Notwithstanding the availability of sufficient assets of the Issuer to pay the Liquidating Distribution, if, at the time the Liquidating Distribution is to be paid, proceedings have been commenced for the winding-up of the Bank in England other than pursuant to a Permitted Reorganisation, the Liquidating Distribution paid to Holders shall not exceed the amount per security that would have been paid as a liquidation distribution out of the assets of the Bank had the Preferred Securities been directly issued preference shares issued by the Bank with equivalent rights of participation in the capital of the Bank (whether or not the Bank could in fact have issued such securities) and ranked (i) junior to depositors and all other creditors (including the holders of subordinated debt) of the Bank, (ii) *pari passu* with all Parity Obligations of the Bank and (iii) senior to the holders of the Bank's ordinary shares and any other securities or obligations of the Bank which are subordinated to the Guarantee.

3.2 If the Liquidating Distribution and any other such liquidation distributions cannot be made in full by reason of the limitation described in paragraph 3.1 or any equivalent article or term of a Parity Obligation, but there are funds available for payment so as to allow payment of part of the Liquidating Distribution then each Holder will be entitled to receive the Relevant Proportion of the Liquidating Distribution. After payment of the Liquidating Distribution, or the Relevant Proportion thereof, if applicable, Holders will have no right or claim to any of the remaining assets of the Issuer or against the Bank under the Guarantee and the holder of the Preferential Right shall be entitled to receive any remaining assets of the Issuer.

3.3 In the event that proceedings are commenced for the liquidation, dissolution or winding up of the Bank in England other than pursuant to a Permitted Reorganisation, the General Partner shall file a statement of dissolution of the Issuer with the Limited Partnerships Registrar and the amount to which Holders shall be entitled as a Liquidating Distribution will be as set out in paragraphs 3.1 and 3.2.

3.4 Subject to paragraph 3.3, unless (i) the FSA has given its consent, if then required, and (ii) the aggregate of (a) the Adjusted Distributable Reserves of the Bank as at the date of such winding up and (b) the proceeds available from an issue of Replacement Capital that has been made for the purpose of funding the Liquidating Distribution is at least equal to the aggregate Liquidating Distribution, the General Partner will not permit, or take any action that would or might cause, the dissolution or winding up of the Issuer. Notwithstanding the foregoing restriction imposed on the General Partner, if for any other reason the Issuer is dissolved or wound up in circumstances where proceedings have not been commenced for the winding up of the Bank, the Liquidating Distribution shall only be payable up to an amount equal to the aggregate of (ii)(a) and (b) above. No Holder shall have any claim (whether against the Issuer or under the Guarantee) in respect of any Liquidating Distribution or part thereof not paid when it would, but for the operation of this paragraph 3.4, otherwise have become due.

3.5 Paragraph 3.4 will not apply in circumstances where a Substitution Event has occurred and the Substitute Preference Shares have been issued.

4. Redemption and Purchase

4.1 The Preferred Securities have no fixed final redemption date and Holders have no rights at any time to call for the redemption of the Preferred Securities.

4.2 The Preferred Securities may be redeemed, in whole but not in part, at the option of the General Partner, subject to the satisfaction of the Redemption Conditions, paragraph 7.3 and to the Law, on any Optional Redemption Date upon not less than 30 nor more than 60 days' notice to the Holders specifying the Optional Redemption Date (which notice shall be irrevocable) at the Optional Redemption Price. Upon the expiry of such notice, the Preferred Securities shall be redeemed by payment of the Optional Redemption Price to the Holders.

4.3 If at any time a Tax Event has occurred and is continuing then either (i) the General Partner may (provided that proceedings have not been commenced for the liquidation, dissolution or winding up of the Bank in England) elect to substitute the Substitute Preference Shares for the Preferred Securities in the manner provided in paragraph 5 as if such event were a Substitution Event; or (ii) the Preferred Securities may be redeemed, in whole but not in part, at the option of the General Partner, subject to the satisfaction of the Redemption Conditions, paragraph 7.3 and to the Law, at any time upon not less than 30 nor more than 60 days' notice to the Holders specifying the Early Redemption Date (which notice shall be irrevocable), at the Tax Redemption Price. Where a notice of redemption has been given in accordance with the foregoing sentence, the General Partner shall also notify the Holders of the Tax Redemption Price as soon as reasonably practicable after it has been determined (and in any event not later than the second Business Day before the Early Redemption Date). Prior to the publication of any notice of redemption pursuant to the foregoing, the General Partner shall deliver to the Registrar a certificate signed by two Directors of the Bank stating that the Issuer is entitled to effect such redemption and an opinion of counsel to the Bank experienced in such matters to the effect that a Tax Event has occurred (and specifying which of paragraphs (i) to (iv) as set out in the definition of "Tax Event" is applicable). The delivery of such opinion shall constitute conclusive evidence of the occurrence of a "Tax Event" for all purposes of the Partnership Agreement and Preferred Securities. Upon the expiry of such notice, the Preferred Securities shall be redeemed by the payment of the Tax Redemption Price to the Holders.

4.4 If at any time a Regulatory Event has occurred and is continuing, either (i) the General Partner may (provided that proceedings have not been commenced for the liquidation, dissolution or winding up of the Bank in England) elect to substitute the Substitute Preference Shares for the Preferred Securities in the manner provided in paragraph 5 as if such event were a Substitution Event or (ii) the Preferred Securities may be redeemed, in whole but not in part, at the option of the General Partner, subject to satisfaction of the Redemption Conditions, paragraph 7.3 and to the Law, at any time upon not less than 30 nor more than 60 days' notice to the Holders specifying the Early Redemption Date (which notice shall be irrevocable), at the Regulatory Event Redemption Price. Where a notice of redemption has been given in accordance with the foregoing sentence, the General Partner shall also notify the Holders of the Regulatory Event Redemption Price as soon as reasonably practicable after it has been determined (and in any event not later than the second Business Day before the Early Redemption Date). Prior to the publication of any notice of redemption pursuant to the foregoing, the General Partner shall deliver to the Registrar a certificate signed by two Directors of the Bank stating that the Issuer is entitled to effect such redemption and an opinion of counsel to the Bank experienced in such matters to the effect that a Regulatory Event has occurred. Upon the expiry of such notice, the Preferred Securities shall be redeemed by the payment of the Regulatory Event Redemption Price to the Holders.

4.5 Under FSA requirements at the date hereof, the Issuer may not redeem, and neither the Issuer nor the Bank nor any of its Subsidiaries may purchase, any Preferred Securities unless the FSA gives its prior written consent, and the FSA may impose conditions on any such redemption or purchase. These requirements and restrictions do not affect the ability of the Bank or its Subsidiaries to engage in market-making activities in relation to the Preferred Securities.

4.6 Once a notice to redeem the Preferred Securities has been given under any of paragraphs 4.2, 4.3 or 4.4, no similar notice may be given under either of the other paragraphs. If at any time the Preferred Securities may be redeemed under more than one such paragraph, the General Partner may elect under which paragraph the notice of redemption is to be given.

5. Substitution by Substitute Preference Shares

5.1 As soon as reasonably practicable following the occurrence of a Substitution Event (provided that proceedings have not been commenced for the liquidation, dissolution or winding up of the Bank in England), the General Partner on behalf of the Issuer shall take all reasonable steps to cause the substitution for the Preferred Securities of fully-paid non-cumulative redeemable perpetual preferred shares issued directly by the Bank having economic terms which are in all material respects equivalent (as more fully set out in the following paragraph) to those of the Preferred Securities and the Guarantee taken together (the "Substitute Preference Shares").

The Substitute Preference Shares shall, among other things, provide economic terms that are equivalent to those of the Preferred Securities in respect of the non-cumulative nature of the distributions thereon, the status of the Preferred Securities and the rights attaching to the Preferred Securities in respect of rights on a winding up of the Bank. The Substitute Preference Shares shall be redeemable or effectively redeemable and will contain provisions similar to those contained in paragraphs 2.2 and 4.2.

5.2 Prior to the issue of any Substitute Preference Shares, application will be made by the Bank for admission of such Substitute Preference Shares to be admitted to listing on the Official List of the UK Listing Authority and to trading on the London Stock Exchange or another Recognised Stock Exchange. As soon as practicable after the occurrence of a Substitution Event (provided that proceedings have not been commenced for the winding up of the Bank in England), the Bank will give written notice to the Holders enclosing a substitution confirmation which each Holder will be required to complete. To receive Substitute Preference Shares, each Holder must deliver to the Paying Agent the duly completed substitution confirmation together with the certificate evidencing its holding of Preferred Securities. Any such substitution shall be effected subject in each case to any applicable fiscal laws or other laws or regulations. Following such substitution, the allotted Substitute Preference Shares will rank, for any dividend from the Distribution Date, immediately preceding the allotment of the Substitute Preference Shares. From the Substitution Event Date, the Holder (a "Former Holder") (a) will have no entitlement to any accrued Distribution or any other payment on, or right in respect of, the Preferred Securities, (b) will be removed from the Register and all rights of the Former Holder to participate in the assets of the Issuer or to be returned any amount in respect of the Preferred Securities (including the Preferred Capital Contribution made by or on behalf of the Former Holder) will be extinguished and (c) shall cease to be a limited partner of the Issuer. If (i) Substitute Preference Shares are issued upon a Substitution Event, the Bank will confer upon Holders the option (A) to receive such Substitute Preference Shares in certificated form or (B) subject to such Holders agreeing to pay any UK stamp duty or stamp duty reserve tax ("SDRT") which would arise on the issue of the Substitute Preference Shares and providing appropriate indemnities against any such stamp duty or SDRT, to require the Bank to issue such Substitute Preference Shares to a clearing system (or a nominee for such clearing system), or if (ii) Substitute Preference Shares are issued other than upon a Substitution Event, the Bank will (A) issue such Substitute Preference Shares to a clearing system or a nominee for such clearing system and (B) pay any UK stamp duty or SDRT payable on the issue of Substitute Preference Shares.

5.3 Certificates (if any) for Substitute Preference Shares issued on substitution will be dispatched by mail free of charge (but uninsured and at the risk of the person entitled thereto) within one month after receipt of a duly completed substitution confirmation. If Substitute Preference Shares are required to be issued, Holders will continue to be entitled to receive Distributions and/or a Liquidating Distribution in respect of the Preferred Securities until the Substitution Event Date. Thereafter the Former Holders will have no further rights, title or interest in or to their Preferred Securities. Upon an involuntary dissolution of the Issuer occurring after the occurrence of a Substitution Event but prior to the Substitution Event Date, Holders will have no further rights, title or interest in or to Preferred Securities except the right to have their respective Preferred Securities substituted in the manner described above.

6. Additional Amounts

All payments in respect of the Preferred Securities by the Issuer will be made without withholding or deduction for, or on account of, any tax imposed by the United Kingdom or Jersey, unless the withholding or deduction of such tax is required by law. In the event of such withholding or deduction, each Holder will, if permitted by the FSA, be entitled to receive, as a further Distribution, such additional amounts ("**Additional Amounts**") as may be necessary in order that the net amounts received by the Holders after such withholding or deduction shall equal the amounts which would have been receivable in respect of the Preferred Securities in the absence of such withholding or deduction; except that no such Additional Amounts will be payable to a Holder (or to a third party on his or her behalf) with respect to any Preferred Security:

6.1 where the Holder is liable to such tax, duty or charge by reason of such Holder having some connection with the jurisdiction by which such tax, duty or charge has been imposed other than the mere holding of such Preferred Security; or

6.2 if such withholding or deduction may be avoided by complying with any statutory requirement or by making a declaration of non-residence or other similar claim for exemption to any authority of or in the United Kingdom or Jersey, unless such Holder proves that he is not entitled so to comply or to make such declaration or claim; or

6.3 if the Holder (or the third party to whom payment is made on behalf of the Holder) is a partnership or is not the sole beneficial owner of the Preferred Security, or holds the Preferred Security in a fiduciary capacity, to the extent that any of the members of the partnership, the beneficial owner or the settlor or beneficiary with respect to the fiduciary would not have been entitled to the payment of an additional amount had each of the members of the partnership, the beneficial owner, settlor or beneficiary (as the case may be) received directly his beneficial or distributive share of the payment; or

6.4 where presentation is required presented for payment more than 30 days after the relevant Distribution Date, except to the extent that the Holder thereof would have been entitled to such Additional Amounts if it had presented the same for payment on the last day of such period of 30 days; or

6.5 where presentation is required if such withholding or deduction may be avoided by presenting the relevant Preferred Security to another Paying Agent; or

6.6 if such withholding or deduction is imposed on or in respect of a payment to an individual Holder and is required to be made pursuant to Council Directive 2003/48/EC of 3 June 2003 on the taxation of savings income in the form of interest payments or any European Union Directive otherwise implementing the conclusions of the ECOFIN Council meeting of 26-27 November 2000 or any law implementing, or complying with, or introduced in order to conform to, any such Directive,

provided that the Issuer's obligation to make any such payments is subject to the Law and to the limitations provided in paragraphs 2.3, 3.1 and 3.4.

7. Payments

7.1 Distributions will be payable subject to the Law on the relevant Distribution Date (or, where any Distribution Date is not a Business Day, on the next Business Day immediately following the Distribution Date, without interest in respect of such delay) to the Holders five Business Days prior to the relevant Distribution Date (the "Relevant Record Date"). If the General Partner gives a notice of redemption pursuant to paragraph 4.2, 4.3 or 4.4 in respect of the Preferred Securities, then, on the Redemption Date, the General Partner shall procure that the Optional Redemption Price, the Tax Redemption Price or the Regulatory Event Redemption Price, as the case may be, will be paid by the Registrar or by the Paying Agents on behalf of the Issuer to the Holders. Upon such payment, all rights of Holders to participate in the assets of the Issuer or to be returned any amount in respect of the Preferred Securities (including the Preferred Capital Contribution made by or on behalf of the Holders) will be extinguished and each Holder shall thereupon cease to be a limited partner of the Issuer provided its holding of Preferred Securities is redeemed in accordance with the foregoing and the Preferred Capital Contribution will, on payment of the Optional Redemption Price, the Tax Redemption Price or the Regulatory Event Redemption Price, as the case may be, be deemed repaid.

7.2 Subject to all applicable fiscal or other laws and regulations:

7.2.1 each payment in respect of Distributions will be made by cheque and mailed on the relevant Distribution Date to the Holder of record at such Holder's address as it appears on the Register on the Relevant Record Date for the Preferred Securities; and

7.2.2 any payment of amounts in respect of the Optional Redemption Price, the Tax Redemption Price, the Regulatory Event Redemption Price or the Liquidating Distribution (or relevant proportion thereof) in respect of any Preferred Security will be made by pounds sterling cheque drawn on a bank in London against presentation and surrender of the relevant certificate of entitlement at the office of the Registrar or any Paying Agent,

provided, however, that a Holder may receive such payment by direct transfer to a pounds sterling account maintained by the Holder with a bank in London arranged by a Paying Agent if appropriate direct transfer instructions have been received by the Registrar in sufficient time prior to the relevant date of payment. Holders will not be entitled to any interest or other payment for any delay after the due date in receiving the amount due if the due date is not a Business Day, if the Holder is late in surrendering certificates (if required to do so) or if a cheque mailed in accordance with this paragraph arrives after the due date for payment.

In the event that payment of the Optional Redemption Price, the Tax Redemption Price or the Regulatory Event Redemption Price is improperly withheld or refused and not paid by the Issuer, Distributions on such Preferred Security, subject as described in paragraph 2.3 and 2.9, will continue to accrue, on a day by day basis compounding annually, from the Redemption Date to the date of actual payment of the Optional Redemption Price, the Tax Redemption Price or the Regulatory Event Redemption Price, as the case may be.

7.3 The Issuer will not, and the Bank has undertaken in the Guarantee that it will not and it will procure that no member of the Bank Group will, make or procure any payment to Holders, if such a payment could not lawfully have been made had Holders held shares ranking *pari passu* with Substitute Preference Shares instead of the Preferred Securities.

7.4 The Issuer will, and the Bank has undertaken in the Guarantee that it will procure that the Issuer will, maintain at all times whilst the Preferred Securities are in issue (a) a Paying Agent outside the European Union and Jersey or in a Member State of the European Union that will not be obliged to withhold or deduct for or on account of tax pursuant to Council Directive 2003/48/EC of 3 June 2003 on the taxation of savings income in the form of interest payments or any European Union Directive otherwise implementing the conclusions of the ECOFIN Council meeting of 26 and 27 November 2000 or any law implementing or complying with, or introduced in order to conform to, any such Directive, (b) for so long as the Preferred Securities are listed on the Luxembourg Stock Exchange, a Paying Agent in Luxembourg, and (c) a Registrar having its office outside the United Kingdom.

8. Voting Rights

8.1 Except as described below and provided for in the Law, Holders will not be entitled to receive notice of or attend or vote at any meeting of partners of the Issuer or participate in the management of the Issuer.

8.2 If for any single Distribution Period ending on or before the First Optional Redemption Date or thereafter for any two consecutive Distribution Periods:

8.2.1 Distributions have not been paid in full on the Preferred Securities by the Issuer; and/or

8.2.2 the Bank has not made the required payments under the Guarantee in respect of such Distributions,

then the Holders together with the holders of any other preferred securities of the Issuer having the right to vote for the election of a special representative (the "Special Representative") in such event, acting as a single class without regard to class, will be entitled to appoint a Special Representative, by written notice to the Issuer given by the holders of a majority by outstanding nominal amount of such Preferred Securities and any other preferred securities having the said right or by resolution passed by the holders of a majority by outstanding nominal amount of such Preferred Securities and any other such preferred securities present in person or by proxy at a separate general meeting of such holders convened for the purpose. The Special Representative shall be authorised to represent the Holders to enforce their statutory rights as limited partners including the provision of information on the affairs of the Issuer; however, it has no rights in addition to those held by Holders. The Special Representative shall not, by virtue only of acting in such capacity, be admitted or authorised to act as a general partner in relation to the Issuer or be admitted as a Holder or otherwise be deemed to be a general partner or a Holder in the Issuer and shall have no liability for the debts, obligations or liabilities of the Issuer or for any unpaid contribution of a partner in its capacity as Special Representative.

Not later than 30 days after such entitlement arises, if the written notice of the Holders of outstanding Preferred Securities and the holders of any other preferred securities of the Issuer having the right to vote for the election of a Special Representative in the circumstances described in the preceding paragraph has not been given as provided for in the preceding paragraph, the General Partner will convene a separate general meeting for the purpose. If the General Partner fails to convene such meeting within such 30-day period, the Holders of 10% by outstanding nominal amount of the Preferred Securities and such other preferred securities will be entitled to convene such a meeting for the purpose. The Partnership Agreement contains provisions concerning the convening and conduct of meetings of Holders. Any Special Representative so appointed shall, subject to the terms of such other preferred securities, vacate office if, after its appointment a full Distribution is made by the Issuer or by the Bank under the Guarantee for one Distribution Period or an amount equivalent to the Distributions to be paid in respect of one Distribution Period has been paid or irrevocably set aside in a separately designated trust account for payment to the Holders.

8.3 The consent in writing of the Holders of at least one-third of the outstanding Preferred Securities or the sanction of a resolution, passed by a majority of at least three-quarters of those present in person or by proxy at a separate meeting of the Holders at which the quorum shall be one or more Holders holding at least one-third in nominal amount of the issued Preferred Securities, shall be required in order to give effect to any variation or abrogation of the rights, preferences and privileges of the Preferred Securities by way of amendment of the Partnership Agreement or otherwise (including, without limitation, the authorisation or creation of any securities or ownership interests of the Issuer ranking, as to participation in the profits or assets of the Issuer, senior to the Preferred Securities), unless otherwise required by applicable law. No such sanction shall be required if the change is solely of a formal, minor or technical nature or is to correct an error or cure an ambiguity, provided that the change does not reduce the amounts payable to Holders, impose any obligation on the Holders or adversely affect their voting rights.

8.4 Notwithstanding the foregoing, no vote of the Holders will be required for the redemption, cancellation or substitution of the Preferred Securities in accordance with the Partnership Agreement.

8.5 Subject to the Law, the Issuer may not be dissolved by the General Partner whilst any Preferred Security is in issue, unless all the Holders and the General Partner have approved such action. Such approval shall not be required if the dissolution of the Issuer is proposed or initiated because of the liquidation, dissolution or winding-up, as the case may be, of the General Partner or the Bank.

8.6 Any Preferred Security, and any preferred security of a type referred to in paragraph 8.2, that is at any time owned by the Bank, or any entity of which the Bank, either directly or indirectly, owns 20% or more of the voting shares or similar ownership interests, shall not carry a right to vote in a meeting of Holders or at any meeting called to vote for the election of a Special Representative pursuant to paragraph 8.2 and shall, for voting purposes, be treated as if it were not in issue other than in the case of the approval required by paragraph 8.5.

8.7 The General Partner will cause a notice of any meeting at which Holders are entitled to vote and any voting forms to be mailed to each Holder. Each such notice will include a statement setting forth (a) the date, time and place of such meeting, (b) a description of any resolution to be proposed for adoption at such meeting on which such Holders are entitled to vote and (c) instructions for the delivery of proxies.

9. Covenant of the General Partner

9.1 The General Partner has undertaken not to incur any indebtedness in the name of the Issuer other than costs and expenses incidental to creating the Preferred Securities (which may include fees and commissions payable in respect of the issue, subscription and sale of the Preferred Securities) and the Issuer, performing its obligations in respect of the Partnership Agreement, maintaining the listing of the Preferred Securities, the Register, the Registrar and Paying Agents in respect of the Preferred Securities, its holding of the Subordinated Note or any Replacement Debt and the maintenance of a custodian thereof, the exercise of the Issuer's rights in respect of the Subordinated Note or any Replacement Debt and the administration of the Issuer.

9.2 The General Partner has undertaken that if the Subordinated Note is redeemed while the Preferred Securities remain outstanding and are not subject to a notice of redemption, it will invest the proceeds of the Subordinated Note or any Replacement Debt in a subordinated note issued by the Bank, with a maturity date of 30 November 2048 and economic terms essentially equivalent to the Subordinated Note (including that the interest rate will reflect the then current Distribution Rate provisions of the Preferred Securities) (the "Replacement Debt").

10. Notices

All notices to the Holders will be mailed to the Holders of record at their respective addresses in the Register and shall be deemed to have been given on the weekday (being a day other than a Saturday or a Sunday) after the date of mailing *provided however, that*, so long as the Preferred Securities are listed on the Stock Exchange (and the rules of that exchange so require), notices will also be published in a leading newspaper having general circulation in Luxembourg (which is expected to be *Luxemburger Wort*). Any such notice shall be deemed to have been given on the date of such publication or, if published more than once or on different dates, on the first date on which such publication is made.

11. Transfers and Form

11.1 The Preferred Securities will be issued in registered form.

11.2 The Preferred Securities will be evidenced by a permanent global certificate in fully registered form (the "Global Certificate") and will be registered in the name of a nominee of, and deposited with a common depositary for, Clearstream, Luxembourg and Euroclear.

11.3 Except in the limited circumstances described below, owners of interests in the Preferred Securities evidenced by a Global Certificate will not be entitled to receive physical delivery of definitive certificates. The Preferred Securities and certificates are not issuable in bearer form.

11.4 If (i) either of Euroclear or Clearstream, Luxembourg is closed for business for a continuous period of 14 days or more (other than for purposes of a public holiday) or announces an intention permanently to cease business or does in fact do so, or (ii) as a result of a change in law, transfer duties or similar taxes become payable on transfers of the Preferred Securities in Euroclear and/or Clearstream, Luxembourg, the Issuer will issue individual definitive certificates in respect of Preferred Securities in registered form in exchange for the Global Certificate. Upon receipt of such notice from Euroclear and/or Clearstream, Luxembourg, the Issuer will use its best efforts to make arrangements with Euroclear and Clearstream, Luxembourg for the exchange of the Global Certificate for individual definitive certificates and cause the requested individual definitive certificates to be executed and delivered to the Registrar in sufficient quantities and authenticated by the Registrar for delivery to holders of Preferred Securities. Persons exchanging interests in the Global Certificate for individual definitive certificates will be required to provide the Registrar with written instructions and other information required by the Issuer and the Registrar to complete, execute and deliver such individual definitive certificates and to make appropriate entries in the Register in respect of the Preferred Securities. In all cases, definitive certificates delivered in exchange for a Global Certificate or an interest in the Preferred Securities evidenced thereby will be registered in the names, and issued in any approved denominations, requested by Euroclear and Clearstream, Luxembourg.

11.5 If definitive certificates are made available in respect of Preferred Securities they will be available from the Registrar and from the Paying Agent at its specified offices, and will be posted to the relevant Holders at the address shown in the Register or, as applicable, in the relevant instrument of transfer within three Business Days of issue, by uninsured post at the risk of such Holders. Transfers of Preferred Securities if evidenced by definitive certificates may be effected by presentation of the relevant certificate (with the transfer certificate relating thereto duly completed on behalf of the transferor and the transferee) at the specified office of the Registrar or the Paying Agent. Where a Holder transfers only some of the Preferred Securities evidenced by any such certificate he shall be entitled to a certificate for the balance without charge. Holders will not be required to bear the costs and expenses of effecting any registration of transfer as provided above, except for any costs or expenses of delivery other than by regular uninsured mail and except that the Issuer may require the payment of a sum sufficient to cover any stamp duty, tax or other governmental charge that may be imposed in relation to the registration.

12. Replacement Certificates

If a certificate is damaged or defaced or alleged to have been lost, stolen or destroyed, a new certificate evidencing the same Preferred Securities may be issued on payment of such fee and on such terms (if any) as to evidence and indemnity and the payment of out-of-pocket expenses as the General Partner may think fit and on payment of the costs of the General Partner incidental to its investigation of the evidence and, if damaged or defaced, on surrendering the old certificate at the specified office of the Paying Agent.

13. Prescription

Unclaimed Distributions, Optional Redemption Price, Tax Redemption Price, Regulatory Event Redemption Price and Liquidating Distributions will be prescribed after ten years in accordance with Jersey law.

14. Governing Law

The Preferred Securities and the Partnership Agreement shall be governed by, and construed in accordance with, Jersey law. Determinations in respect of amounts of Adjusted Distributable Reserves shall, however, be made in accordance with English law.

SUMMARY OF PROVISIONS RELATING TO THE PREFERRED SECURITIES IN GLOBAL FORM

Initial Issue of Preferred Securities

The Preferred Securities will be issued in registered form and will be initially evidenced by interests in a Global Certificate which will be registered in the name of a nominee of, and deposited with a common depositary for, Euroclear and Clearstream, Luxembourg on the Issue Date. Upon the registration of Preferred Securities in the name of a nominee of Euroclear and Clearstream, Luxembourg and delivery of the Global Certificate to the common depositary for Euroclear and Clearstream, Luxembourg, Euroclear or Clearstream, Luxembourg will credit each subscriber with such number of Preferred Securities as is equal to the number thereof for which it has subscribed and paid.

Accountholders

So long as the Preferred Securities are registered in the name of a nominee for Euroclear and Clearstream, Luxembourg, the nominee for Euroclear and Clearstream, Luxembourg will be the sole registered owner or holder of the Preferred Securities evidenced by the Global Certificate for all purposes under the Partnership Agreement. Except as set forth under "*Description of Preferred Securities – Transfers and Form*" and under "*– Transfers of Interests*", the persons shown in the records of Euroclear, Clearstream, Luxembourg or any other clearing system (an "*Alternative Clearing System*") as the holders of the Preferred Security evidenced by the Global Certificate (each an "*Accountholder*") will not be entitled to have Preferred Securities registered in their names, will not receive or be entitled to receive physical delivery of definitive certificates evidencing interests in the Preferred Securities and will not be considered registered owners or holders thereof under the Partnership Agreement. Accordingly, each Accountholder must rely on the rules and procedures of Euroclear and Clearstream, Luxembourg, as the case may be, to exercise any rights and obligations of a holder of Preferred Securities under the Partnership Agreement.

Payments

Each Accountholder must look solely to Euroclear, Clearstream, Luxembourg or such Alternative Clearing System, as the case may be, for its share of each payment made by the Issuer to the registered holder of the Preferred Securities and in relation to all other rights arising under the Global Certificate, subject to and in accordance with the respective rules and procedures of Euroclear, Clearstream, Luxembourg or such Alternative Clearing System, as the case may be. Such persons shall have no claim directly against the Issuer in respect of payments due on the Preferred Securities for so long as the Preferred Securities are evidenced by such Global Certificate and such obligations of the Issuer will be discharged by payment to the registered holder of the Preferred Securities in respect of each amount so paid.

Transfers of Interests

Accountholders will only be able to transfer their beneficial interests in the Preferred Securities in accordance with the rules and procedures of Euroclear, Clearstream, Luxembourg or the Alternative Clearing System, as the case may be.

Settlement

Initial settlement for the Preferred Securities and settlement of any secondary market trades in the Preferred Securities will be made in same-day funds.

DESCRIPTION OF THE GUARANTEE

The following is the form of the Guarantee to be executed by the Bank:

THIS DEED OF GUARANTEE (the "**Guarantee**"), dated 5 November 2003, is executed and delivered by HSBC Bank plc (the "**Bank**") for the benefit of the Holders (as defined below).

WHEREAS:

(a) the Bank desires to issue this Guarantee for the benefit of the Holders, as provided herein; and

(b) this Guarantee is intended to provide the Holders, on a dissolution or winding up of the Issuer (as defined below) or on a default by the Issuer in discharging its obligations in respect of the Preferred Securities (as defined below), with rights against the Bank in respect of the Guaranteed Payments (as defined below) which are as nearly as possible equivalent to those which they would have had if the Preferred Securities had been directly issued non-voting, non-cumulative, preference shares of the Bank (whether or not the Bank could in fact have issued such shares).

NOW, THEREFORE, the Bank executes and delivers this Guarantee as a deed poll for the benefit of the Holders.

1. Definitions

As used in this Guarantee, capitalised terms not defined herein shall have the meanings ascribed to them in the Partnership Agreement and otherwise the following terms shall, unless the context otherwise requires, have the following meanings:

"Guaranteed Payments" means collectively (i) all Distributions due on the Preferred Securities, (ii) any Distributions on the Preferred Securities which would have been due had the Issuer had sufficient legally available resources but only if, and to the extent that, the Issuer did not have such legally available resources solely due to a failure by the Bank to pay interest on the Subordinated Note or the Replacement Debt as and when due and payable under the terms thereof, (iii) any Liquidating Distribution, (iv) any amounts to which the Holders are entitled in respect of redemption of the Preferred Securities and (v) any Additional Amounts;

"Holder" means, in respect of each Preferred Security, the person registered on the Register as the limited partner holding such Preferred Security at the relevant time;

"Issuer" means HSBC Bank Capital Funding (Sterling 1) L.P.;

"Partnership Agreement" means the Limited Partnership Agreement dated 31 October 2003 between, *inter alia*, HSBC Bank (General Partner) Limited (the "General Partner"), HSBC Issuer Services Common Depositary Nominee (UK) Limited (the "Initial Partner") and HSBC Preferential LP (UK) (the "Preferential Limited Partner") establishing the Issuer;

"Preferred Securities" means collectively the £700,000,000 5.844% Non-cumulative Step-up Perpetual Preferred Securities of the Issuer, whether or not in issue on the date of this Guarantee, the Holders of which are entitled to the benefits of this Guarantee as evidenced by the execution of this Guarantee;

"Solvent" means, in relation to the Bank, that its Assets exceed its Liabilities (in each case, as defined below) excluding its Liabilities to persons in respect of Subordinated Indebtedness whose claims rank or are expressed to rank *pari passu* with, or junior to, the Guarantee or any other of its obligations which rank *pari passu* with, or junior to, the Guarantee; and "Insolvent" shall be construed accordingly, and for the purposes hereof, "Assets" means the unconsolidated gross assets (including contingencies) of the Bank and "Liabilities" means the unconsolidated gross liabilities (including contingencies) of the Bank, all as shown in the latest published balance sheet having the benefit of an unqualified auditors' report but with such adjustments as the auditors of the Bank or, if the Bank is in winding up, the liquidator shall determine in any report of such auditor issued on the request of the Bank or of such liquidator prepared in connection with the liquidation of the Bank and in either case relating to the solvency of the Bank; and

"Subordinated Indebtedness" means any liability of the Bank howsoever arising for the payment of money the right to payment of which by the Bank by the terms thereof is, or is expressed to be, subordinated in the event of a winding up of the Bank to the claims of all or any of the creditors of the Bank; provided that the term "Subordinated Indebtedness" shall include, without limitation, any liability of the Bank to any creditor of the Bank:

(i) whose right to payment ranks or is expressed to rank postponed or subordinated to that of unsubordinated creditors (such unsubordinated creditors not being creditors whose right to payment is preferred by operation of law); or

(ii) whose right to payment is made subject to a condition or is restricted (whether by operation of law or otherwise) or is expressed to be restricted in each case such that the amount which may be claimed for his own retention by such creditor in the event that the Bank is not Solvent is less than in the event that the Bank is Solvent.

2. Guarantee

2.1 Subject to the exceptions and limitations contained in the following provisions of this Clause 2, the Bank irrevocably guarantees to the Holders the payment in full of the Guaranteed Payments, as and when due, to the extent that such payments shall not have been paid when due and payable by the Issuer regardless of any defence, right of set-off or counterclaim which the Issuer may have or assert. This Guarantee is continuing, irrevocable and absolute. The rights of the Holders against the Bank under this Guarantee will, in the event of the winding up of the Bank, be subordinated in right of payment to the claims of all other creditors of the Bank other than creditors in respect of Subordinated Indebtedness whose claims rank or are expressed to rank *pari passu* with or junior to the Guarantee or any other of the Bank's obligations which rank *pari passu* with or junior to the Guarantee.

2.2 Notwithstanding Clause 2.1, the Bank's obligation to make any Guaranteed Payment is conditional upon it being able to make such payment and be Solvent immediately thereafter and, furthermore, the Bank will not, save to the extent provided in Clause 2.5, be obliged to make payment under the Guarantee of any Guaranteed Payment if the Bank is prevented by applicable UK banking regulations or other requirements from making such payment in full under this Guarantee. In addition, notwithstanding Clause 2.1, the Bank will not, save to the extent provided in Clause 2.5, be obliged to make payment under the Guarantee of any Guaranteed Payment in respect of Distributions on any Preferred Securities if, on the relevant Distribution Date:

(a) the Bank is prevented by applicable UK banking regulations or other requirements from making payment in full of dividends or other distributions due and payable on its Parity Obligations or is unable to make such payment of dividends or other distributions on its Parity Obligations without causing a breach of the FSA's capital adequacy requirements from time to time applicable to the Bank; or

(b) the amount of the Distribution to which such Guaranteed Payment relates (if paid in full), together with the sum of any dividends and other distributions on the Bank's Parity Obligations due and payable on the Distribution Date in respect of such Distribution, would exceed the Adjusted Distributable Reserves of the Bank determined as of the Distribution Determination Date immediately preceding the relevant Distribution Date.

2.3 The Bank will determine whether as of the Distribution Determination Date sufficient Adjusted Distributable Reserves exist to allow a payment of some or all of the relevant Distribution. In the event that any Distribution cannot be paid in full, the Bank will notify or procure notification to the Stock Exchange, the General Partner, the Registrar and the Paying Agent, and to Holders in accordance with the Partnership Agreement, of the fact and of the amount, if any, to be paid in respect of that Distribution.

2.4 All payments under the Guarantee will be made without withholding or deduction for or on account of any present or future taxes, duties, assessments or governmental charges of whatever nature imposed or levied by or on behalf of the United Kingdom or any political sub-division thereof or by any authority therein or thereof having power to tax, unless the withholding or deduction of such taxes, duties, assessments or governmental charges is required by law. In that event, the Bank will, subject to permission (if required) being granted by the FSA, pay such additional amounts ("Guarantor Additional Amounts") as may be necessary in order that the net amounts received by the Holders after such withholding or deduction shall equal the amounts which would have been receivable under this Guarantee in the absence of such withholding or deduction; except that no such Guarantor Additional Amounts will be payable to a Holder (or a third party on his behalf) in respect of any Preferred Security:

(a) where the Holder is liable to such tax, duty or charge by reason of such Holder having some connection with the jurisdiction by which such tax, duty or charge has been imposed other than the mere holding of the relevant Preferred Security; or

(b) if such withholding or deduction may be avoided by complying with any statutory requirement or by making a declaration of non-residence or other similar claim for exemption to any authority of or in the United Kingdom, unless such Holder proves that he is not entitled so to comply or to make such declaration or claim; or

(c) if the Holder (or the third party to whom payment is made on behalf of the Holder) is a partnership or is not the sole beneficial owner of the Preferred Security or holds the Preferred Security in a fiduciary capacity, to the extent that any of the members of the partnership, the beneficial owner or the settlor or beneficiary with respect to the fiduciary would not have been entitled to the payment of an additional amount had each of the members of the partnership, the beneficial owner, settlor or beneficiary (as the case may be) received directly his beneficial or distributive share of the payment; or

(d) where presentation is required presented for payment more than 30 days after the relevant Distribution Date, except to the extent that the Holder thereof would have been entitled to such additional amounts if it had presented the same for payment on the last day of such period of 30 days; or

(e) where presentation is required if such withholding or deduction may be avoided by presenting the relevant Preferred Security to another Paying Agent; or

(f) if such withholding or deduction is imposed on or in respect of a payment to an individual Holder and is required to be made pursuant to Council Directive 2003/48/EC of 3 June 2003 on the taxation of savings income in the form of interest payments or any European Union Directive otherwise implementing the conclusions of the ECOFIN Council meeting of 26-27 November 2000 or any law implementing, or complying with, or introduced in order to conform to, any such Directive,

provided that the Bank's obligation to pay any Guarantor Additional Amounts is subject to the conditions relating to payments under the Guarantee set out in Clauses 2.2 and 2.3.

2.5 In the event that the amounts described in Clauses 2.1 and 2.4 cannot be paid in full by reason of the condition referred to in Clause 2.2, such amount as is to be paid will be payable *pro rata* in the Relevant Proportion and the obligations of the Bank in respect of any such unpaid amount shall lapse.

2.6 The obligations, covenants, agreements and duties of the Bank under this Guarantee shall in no way be affected or impaired by reason of the happening from time to time of any of the following:

(a) the release or waiver, by operation of law or otherwise, of the performance or observance by the Issuer of any express or implied agreement, covenant, term or condition relating to the Preferred Securities to be performed or observed by or on behalf of the Issuer; or

(b) the extension of time for the payment by or on behalf of the Issuer of all or any portion of any Distribution, the Optional Redemption Price, the Tax Redemption Price, the Regulatory Event Redemption Price, the Liquidating Distribution or any other sums payable under the terms of the Preferred Securities or the extension of time for the performance of any other obligation under, arising out of, or in connection with, the Preferred Securities; or

(c) any failure, omission, delay or lack of diligence on the part of Holders to enforce, assert or exercise any right, privilege, power or remedy conferred on the Holders pursuant to the terms of the Preferred Securities, or any action on the part of the Issuer granting indulgence or extension of any kind; or

(d) the voluntary or involuntary winding up, dissolution, amalgamation, reconstruction, sale of any collateral, receivership, insolvency, bankruptcy, assignment for the benefit of creditors, reorganisation, arrangement, composition or readjustment of debt of, or other similar proceedings affecting, the Issuer or any of the assets of the Issuer; or

(e) any invalidity of, or defect or deficiency in, the Preferred Securities; or

(f) the settlement or compromise of any obligation guaranteed hereby or hereby incurred.

There shall be no obligation on the Holders to give notice to, or obtain consent of, the Bank with respect to the happening of any of the foregoing.

2.7 This Guarantee shall be deposited with and held by the Registrar until all the obligations of the Bank have been discharged in full. The Bank hereby acknowledges the right of every Holder to the production of, and the right of every Holder to obtain a copy of, this Guarantee from the Registrar.

2.8 Subject to Clause 2.11 and 2.12, a Holder may enforce this Guarantee directly against the Bank, and the Bank waives any right or remedy to require that any action be brought against the Issuer or any other person or entity before proceeding against the Bank. Subject to Clause 2.12, all waivers contained in this Guarantee shall be without prejudice to the right to proceed against the assets of the Issuer and the General Partner as permitted by the terms of the Preferred Securities. The Bank agrees that this Guarantee shall not be discharged except by complete performance of all obligations of the Bank under this Guarantee.

2.9 The Bank shall be subrogated to any and all rights of the Holders against the assets of the Issuer in respect of any amounts paid to the Holders by the Bank under this Guarantee. The Bank shall not (except to the extent required by mandatory provisions of law) exercise any rights which it may acquire by way of subrogation or any indemnity, reimbursement or other agreement, in all cases as a result of a payment under this Guarantee if, at the time of any such payment, any amounts are due and unpaid under this Guarantee. If the Bank shall receive or be paid any amount with respect to the Preferred Securities in violation of the preceding sentence, the Bank agrees to pay the amount to the Holders.

2.10 The Bank acknowledges that its obligations hereunder are several and independent of the obligations of the Issuer with respect to the Preferred Securities and that the Bank shall be liable as principal and sole obligor hereunder to make the payments undertaken to be made by it pursuant to the terms of this Guarantee, notwithstanding the occurrence of any event referred to in Clause 2.6.

2.11 Following a failure by the Bank to make a payment under this Guarantee on the due date therefor, which failure continues for more than seven days, a Holder or Holders holding not less than one-fifth of the outstanding nominal amount of Preferred Securities may petition for the winding up of the Bank in England and claim in the liquidation of the Bank but no other remedy shall be available to the Holder.

2.12 No Holder shall following any breach by the Bank of any of its obligations under this Guarantee be entitled to exercise any right of set-off or counterclaim which may be available to it against amounts owing by the Bank to such Holder. Notwithstanding the provisions of the foregoing sentence, if any of the said rights and claims of any Holder against the Bank is discharged by set-off, such Holder will immediately pay an amount equal to the amount of such discharge to the Bank or, in the event of its winding-up, the trustee or liquidator of the Bank and until such time as payment is made will hold a sum equal to such amount in trust for the Bank, or the trustee or liquidator of the Bank and accordingly any such discharge will be deemed not to have taken place.

3. Undertakings

3.1 The Bank undertakes that if for any single Distribution Period ending on or before the First Optional Redemption Date or thereafter for any two consecutive Distribution Periods the Distribution is not paid in full to Holders by reason of the limitations set out in the terms of the Preferred Securities and in the Partnership Agreement, the Bank will not (a) declare or pay any dividends or other distributions in respect of its ordinary shares or (if permitted) effect any repurchase of its ordinary shares or any other securities or obligations of the Bank ranking junior to the Guarantee (or contribute any moneys to a sinking fund for the redemption of any such shares or securities) until after the next following Distribution Date on which a Distribution in respect of the Preferred Securities is paid in full (or an amount equivalent to the Distribution to be paid in respect of the next Distribution Period has been paid or irrevocably set aside in a separately designated trust account for payment to the Holders) or (b) (if permitted) repurchase or redeem Parity Obligations which are securities until after the next following Distribution Date on which a Distribution in respect of the Preferred Securities is paid in full (or an amount equivalent to the Distribution to be paid in respect of the next Distribution Period has been paid or irrevocably set aside in a separately designated trust account for payment to the Holders).

3.2 The Bank undertakes that, so long as any of the Preferred Securities are outstanding (a) unless the Bank is itself being wound up, it will not permit, or take any action that would or might cause, the liquidation, dissolution or winding up of the General Partner or the Issuer otherwise than (i) with the prior approval of the FSA (if then required) and (ii) if either (A) the Bank has sufficient Adjusted Distributable Reserves or (B) the Bank has proceeds available from an issue of Replacement Capital that has been made for the purpose of funding the Liquidating Distribution (in either of cases (ii)(A) or (B) in an amount at least equal to the aggregate Liquidating Distribution) and (b) the General Partner will at all times be a directly or indirectly wholly owned subsidiary of the Bank, unless in the case of (a) or (b), otherwise approved by all Holders.

3.3 The Bank undertakes (a) to take all reasonable steps to ensure that it will at all times have a sufficient amount of authorised but unissued Substitute Preference Shares to permit the substitution thereof for all outstanding Preferred Securities and (b) to take all reasonable steps to ensure that all corporate authorisations will have been taken for the allotment and issue of the same free from pre-emptive rights, and that following the occurrence of a Substitution Event and subject to the terms of the Partnership Agreement and the necessary authorisations being in place, it will allot, issue and deliver Substitute Preference Shares in satisfaction of the rights of the Holders in the circumstances described in the Partnership Agreement, such Substitute Preference Shares having the rights and being subject to the conditions set out in the Partnership Agreement. The Bank further undertakes that (a) it will take all reasonable steps to procure that such Substitute Preference Shares will at the relevant time be listed on a Recognised Stock Exchange and (b) if (i) Substitute Preference Shares are issued upon a Substitution Event, the Bank will confer upon Holders the option (A) to receive such Substitute Preference Shares in certificated form or (B) subject to such Holders agreeing to pay any UK stamp duty or stamp duty reserve tax ("SDRT") which would arise on the issue of the Substitute Preference Shares and providing appropriate indemnities against any such stamp duty or SDRT, to require the Bank to issue such Substitute Preference Shares to a clearing system (or a nominee for such clearing system); or if (ii) Substitute Preference Shares are issued other than upon a Substitution Event, the Bank will

(A) issue such Substitute Preference Shares to a clearing system (or a nominee for such clearing system) and (B) pay any UK stamp duty or SDRT payable on the issue of Substitute Preference Shares.

3.4 The Bank undertakes that neither it nor any other member of the Bank Group will make or procure any payment to Holders if such a payment could not lawfully have been made had Holders held shares of the Bank ranking *pari passu* with the Substitute Preference Shares instead of the Preferred Securities.

3.5 The Bank undertakes that it will procure that the Issuer will maintain at all times whilst the Preferred Securities are in issue (a) a Paying Agent outside the European Union and Jersey or in a Member State of the European Union that will not be obliged to withhold or deduct for or on account of tax pursuant to Council Directive 2003/48/EC of 3 June 2003 on the taxation of savings income in the form of interest payments or any European Union Directive otherwise implementing the conclusions of the ECOFIN Council meeting of 26 and 27 November 2000 or any law implementing or complying with, or introduced in order to conform to, any such Directive, (b) for so long as the Preferred Securities are listed on the Luxembourg Stock Exchange, a Paying Agent in Luxembourg, and (c) a Registrar having its office outside the United Kingdom.

3.6 The Bank undertakes that it will not redeem the Subordinated Note pursuant to the Terms and Conditions of the Subordinated Note other than in circumstances where (i) the proceeds of redemption will be invested in Replacement Debt, or (ii) the corresponding Preferred Securities are also being redeemed.

4. Termination

With respect to the Preferred Securities, this Guarantee shall terminate and be of no further force and effect upon (i) payment of the Optional Redemption Price, the Tax Redemption Price, or the Regulatory Event Redemption Price, as the case may be, on all Preferred Securities, (ii) purchase and cancellation of all Preferred Securities, (iii) payment of the Liquidating Distribution, or the Relevant Proportion thereof, or (iv) issue and allotment in full of Substitute Preference Shares, as the case may be, and dissolution of the Issuer, provided however that this Guarantee will continue to be effective or will be reinstated, as the case may be, if at any time payment of any sums paid in respect of the Preferred Securities or under this Guarantee must be restored by a Holder for any reason whatsoever.

5. Transfer; Amendment; Notices

5.1 Subject to operation of law, all guarantees and agreements contained in this Guarantee shall bind the successors, assignees, receivers, trustees and representatives of the Bank and shall inure to the benefit of the Holders. The Bank shall not transfer its obligations hereunder without the prior approval of the Holders of not less than one-third by nominal amount of the Preferred Securities (excluding any Preferred Securities held by the Bank or any entity of which the Bank, either directly or indirectly, owns 20 per cent. or more of the voting shares or similar ownership interests), which approval shall be obtained in accordance with the procedures contained in the Partnership Agreement and the Law.

5.2 Except for those changes (a) required to correct any manifest errors or ambiguities; or (b) which do not materially adversely affect the rights of the Holders (in each of which cases no consent will be required), this Guarantee shall be changed only by the Bank with the consent in writing of the Holders of at least one-third of the outstanding Preferred Securities, or the sanction of a resolution of the Holders of the outstanding Preferred Securities, passed by a majority of at least three-quarters of those present in person or by proxy at a separate meeting of the Holders at which the quorum shall be one or more Holders holding at least one-third in nominal amount of the outstanding Preferred Securities, subject in each case to consent or sanction being obtained in accordance with the procedures contained in the Partnership Agreement and the Law.

5.3 Any notice, request or other communication required or permitted to be given hereunder to the Bank shall be given in writing by delivering the same against receipt therefor or by pre-paid post addressed to the Bank at:

HSBC Bank plc
8 Canada Square
London E14 5HQ

The address of the Bank may be changed at any time and from time to time and shall be the most recent such address furnished in writing by the Bank to the Registrar and notified to the Holders.

Any notice, request or other communication required or permitted to be given hereunder to the Holders shall be given by the Bank in the same manner as notices sent on behalf of the Issuer to Holders.

5.4 This Guarantee is solely for the benefit of the Holders and is not separately transferable from their interests in respect of the Preferred Securities.

5.5 The Bank will furnish any Holder, upon request of such Holder, with a copy of its annual report and any interim reports made generally available by the Bank to holders of the ordinary shares of the Bank.

6. Governing Law

This Guarantee shall be governed by, and construed in accordance with, English law.

IN WITNESS WHEREOF this Guarantee has been executed as a deed poll on behalf of

HSBC Bank plc.

DESCRIPTION OF THE SUBSTITUTE PREFERENCE SHARES

It is intended that the Preference Shares to be issued upon substitution of the Preferred Securities (the "Preference Shares") will have the principal share rights described below.

The rights attaching to the Preference Shares are contained in the Bank's Articles of Association (the "Articles") and in the resolutions to be passed by the Board of Directors of the Bank or a duly constituted committee thereof at or before the time of issue of the Preference Shares. In addition, a detailed description of the rights attaching to the Preference Shares is included in the Partnership Agreement.

Denomination

The par value of each Preference Share will be £1.00 which together with the premium on issue will aggregate to £1,000 or such lesser amount as is equal to the nominal amount of one Preferred Security (the "Principal Amount"). The premium applicable to each Preference Share will be determined by the Board of Directors of the Bank or a duly constituted committee thereof at or before the issue of the Preference Shares. The Preference Shares will be issued credited as fully paid.

Dividends

(a) Subject to sub-paragraphs (e) and (f) below, each Preference Share will entitle the holder thereof to receive a non-cumulative preferential dividend on the Principal Amount thereon calculated on the bases set out in sub-paragraphs (b) and (c) below. The dividend will be payable annually in arrear on 5 November in each year up to and including the relevant Dividend Re-set Date and thereafter semi-annually in arrear on 5 May and 5 November in each year (each a "Dividend Payment Date") when, as and if declared by the Board of Directors, provided that the first dividend will be paid on a *pro rata* basis in respect of the period from, and including, the date of the Distribution Date (as defined in the Partnership Agreement) immediately preceding the date on which the Preference Shares are substituted for the Preferred Securities (the "Substitution Date") to, but excluding, the first such Dividend Payment Date after issue. If any Dividend Payment Date after the Dividend Re-set Date (as defined below) would otherwise fall on a day which is not a Business Day payment of the Dividend otherwise payable on such date will be postponed to the next day which is a Business Day.

    "Dividend Re-set Date" means 5 November 2031.

    Such dividends will only be payable to the extent that payment of the same can be made out of profits available for distribution (the "Distributable Profits") under the provisions of the United Kingdom Companies Act as at each Dividend Payment Date.

    The Preference Shares will rank as regards participation in profits *pari passu inter se* and *pari passu* with any other shares to the extent that they are expressed to rank *pari passu* therewith and in priority to the Bank's ordinary shares and to any other class of shares of the Bank issued after the date of issue of the Preference Shares.

    For the purposes of this Description of the Preference Shares, "Dividend Period" means the period from the date of the Distribution Date immediately preceding the Substitution Date to the first Dividend Payment Date and each successive period from, and including, a Dividend Payment Date to, but excluding, the next succeeding Dividend Payment Date and "Business Day" means a day other than a Saturday or a Sunday on which commercial banks and foreign exchange markets settle payments in pounds sterling and are open for general business in London.

(b) Each Preference Share in issue prior to the Dividend Re-set Date will entitle the holder thereof to receive on each Dividend Payment Date falling on or prior to the Dividend Re-set Date dividends payable in pounds sterling at a fixed rate per annum of 5.844% in respect of the Preference Shares of the Principal Amount thereof calculated on the basis of the actual number of days in the relevant period divided by 365 (or, if any portion of the relevant period falls in a leap year, the sum of (a) the actual number of days in that portion of the relevant period falling in a leap year divided by 366 and (b) the number of days in that portion of the relevant period falling in a non-leap year divided by 365).

(c) Each Preference Share in issue on or after the Dividend Re-set Date will entitle the holder thereof to receive dividends payable in pounds sterling at the rate equal to six-month LIBOR in effect during the relevant Dividend Period plus the Margin, applied to the Principal Amount thereof calculated on the basis of the actual number of days in the relevant period divided by 365.

The Reference Rate from time to time in respect of each Preference Shares will be determined in the manner and on the same basis as the Distribution Rate applicable to the Preferred Securities for such period provided, however, that all calculations relating to the Reference Rate will be made by the Bank.

(d) Any decision regarding the declaration or payment of any dividend on the Preference Shares will be at the sole discretion of the Directors and nothing herein contained will impose on the Directors any requirement or duty to resolve to distribute in respect of any financial year or period the whole or any part of the profits of the Bank available for distribution.

(e) Without prejudice to paragraph (d) above, if, in the opinion of the Directors, the distributable profits of the Bank are insufficient to cover both the payment in full of dividends payable on the Preference Shares on any Dividend Payment Date and on all other dividends stated to be payable on such date on any other shares expressed to rank *pari passu* with the Preference Shares as regards participation in profits, then, subject to paragraph (f) below, dividends may be declared by the Directors pro rata on such Preference Shares and on such other shares to the extent of the available distributable profits (if any) to the extent that the amount of dividend declared per share on each such Preference Share and on each such other share will bear to each other the same ratio as the dividends payable on each such Preference Share and on each such other share bear to each other.

(f) If, in the opinion of the Directors, the declaration or payment of any dividend on any Preference Shares would breach or cause a breach of the FSA's capital adequacy requirements from time to time applicable to the Bank and/or any of its subsidiary undertakings, then no such dividend will be declared or paid.

(g) Payments of preferential dividends shall be made to holders on the register at any date selected by the directors up to 42 days prior to the relevant Dividend Payment Date. The Preference Shares will carry no further right as regards participation in the profits of the Bank.

(h) If for any single Dividend Period ending on or before the Dividend Re-set Date, or for any two consecutive Dividend Periods thereafter the dividend is not paid in full the Bank will not (a) declare or pay any dividends or other distributions in respect of its ordinary stock or any other security of the Bank ranking junior to the Preference Shares or (if permitted) effect any repurchase or redemption of its ordinary stock or any other preference shares of the Bank ranking junior to the Preference Shares (or contribute any moneys to a sinking fund for the redemption of such stock or preference shares) until after the next following Dividend Payment Date on which a dividend in respect of the Preference Shares is paid in full (or an amount equivalent to the dividend to be paid in respect of the next Dividend Payment Period has been paid or set aside for payment to the holders of the Preference Shares) or (b) (if permitted) repurchase or redeem any other preference shares which rank *pari passu* with the Preference Shares until after the next following Dividend Payment Date on which a dividend in respect of the Preference Shares is paid in full (or an amount equivalent to the dividend to be paid in respect of the next Dividend Period has been paid or set aside for payment to the holders).

(i) Any dividend unclaimed after a period of 12 years from the date of declaration of such dividend will be forfeited and revert to the Bank. No dividends or other moneys payable on or in respect of a Preference Share shall bear interest against the Bank.

Return of Capital

(a) On a return of capital in a winding up (but not on a redemption, reduction of capital or purchase of any shares by the Bank) the Preference Shares will rank, *pari passu inter se* and *pari passu* with any other shares of the Bank that are expressed to rank *pari passu* therewith as regards participation in the capital, and otherwise in priority to its ordinary shares and any other class of shares of the Bank ranking junior to the Preference Shares. On such a return of capital, each Preference Share will be entitled to receive in pounds sterling an amount equal to the Principal Amount together with, subject to the restrictions in paragraphs (e) and (f) under "Dividends" above, the amount of (i) any unpaid dividend for any Dividend Period ending on or before the date of commencement of the winding up or other return of capital (the "relevant date") and (ii) a pro rated dividend (calculated on the basis mentioned in (c) under "Dividends" above) in respect of the period, if any, from and including the last Dividend Payment Date prior to the relevant date down to but excluding the relevant date.

(b) If, upon any such return of capital, the amounts available for payment are insufficient to cover the amounts payable in full on the Preference Shares and on any other shares expressed to rank *pari passu* therewith as regards participation in assets, then the holders of the Preference Shares and such other shares will share rateably and proportionately in such return of capital.

(c) No Preference Share will confer any further right to participate on a return of capital of the Bank.

Redemption

(a) Subject to paragraph (f) below, the Bank may, at its option, redeem all, but not merely some, of the Preference Shares for the time being issued and outstanding on the Dividend Re-set Date, and, on each Dividend Payment Date thereafter (each a "Redemption Date") provided that if either of the restrictions mentioned in paragraphs (e) and (f) under "Dividends" above applies to the dividend on the selected Redemption Date, the Bank may not redeem any of the Preference Shares on that Redemption Date.

(b) Any redemption of the Preference Shares will be for cash.

(c) If Preference Shares are to be redeemed, a notice of redemption (a "Redemption Notice") will be mailed to each holder of Preference Shares to be redeemed, not less than 30 Business Days nor more than 60 Business Days prior to the relevant Redemption Date. Each Redemption Notice will specify, *inter alia*, (i) the Redemption Date, (ii) the particular Preference Shares to be redeemed on the Redemption Date, (iii) the Redemption Price and (iv) the place or places where holders may surrender share certificates (if applicable) in respect of such Preference Shares and obtain payment of the Redemption Price. No defect in the Redemption Notice or in its mailing will affect the validity of the redemption proceedings.

The cash amount payable on Redemption (the "Redemption Price") will equal the Principal Amount of such Preference Share. Any such Redemption will not prejudice the rights of the holder of any Preference Share to be so redeemed to receive any accrued but unpaid dividend on that Preference Share payable on the Redemption Date.

(d) Payments in respect of the amount due on redemption of a Preference Share will be made by cheque or upon the written request of the holder or all joint holders not later than the date specified for the purpose in the Redemption Notice by transfer to a pounds sterling account maintained by the payee with a bank in London or such other method as the directors may specify in the Redemption Notice. Payment will be made against presentation and surrender of the relative share certificate (if any) at the place or one of the places specified in the Redemption Notice.

(e) A receipt given by the holder for the time being of any Preference Share (or in the case of joint holders by the first-named joint holder) in respect of the amount payable on redemption of such Preference Share will constitute an absolute discharge to the Bank.

(f) Any redemption of the Preference Shares will be made in compliance with the provisions of the United Kingdom Companies Act, the Uncertificated Securities Regulations and every other statute for the time being in force concerning bodies corporate and affecting the Bank (the "Statutes") and the Articles. No redemption of any Preference Shares may be made by the Bank without the prior consent of the FSA (for so long as the Bank is required to obtain such consent) and subject to such conditions as the FSA may impose at the time of any consent.

Voting

Except as provided below, holders of Preference Shares will not be entitled to attend and vote at general meetings of the Bank. Holders will be entitled to attend and vote at a class meeting of holders of Preference Shares. Every holder of Preference Shares who is present in person at a class meeting of holders of Preference Shares will have one vote on a show of hands and on a poll every holder of Preference Shares who is present in person or by proxy will have one vote for every Preference Share of which he is the holder.

If prior to any general meeting of shareholders of the Bank, dividends in respect of any single Dividend Period prior to the Dividend Re-set Date or for two consecutive Dividend Periods thereafter have not been paid in full, then the holders of the Preference Shares shall have the right to receive notice of, attend, speak and vote at such general meeting on all matters and such right shall continue until after the next following Dividend Payment Date on which a dividend in respect of the Preference Shares is paid in full (or an amount equivalent to the dividend to be paid in respect of the next Dividend Payment Period has been paid or set aside for payment to the holders of the Preference Shares).

Purchases

The Bank may at any time and from time to time exercise any powers conferred by the Statutes in purchasing the Preference Shares. No repurchase of any Preference Shares will be made without the prior consent of the FSA (for so long as the Bank is required to obtain such consent).

Variations of Rights and Further Issues

Subject to the provisions of the Statutes, the special rights attached to any class of shares may be varied or abrogated with the consent in writing of the holders of three-quarters in nominal value of the issued shares of that class or with the sanction of an extraordinary resolution passed at a separate meeting of the holders of shares of that class. At any such separate meeting, the provisions of the Articles relating to general meetings will apply, but the necessary quorum at any such meeting will be two persons at least holding or representing by proxy at least one-third in nominal value of the issued shares of that class (but so that at any adjourned meeting any holders of shares of the class present in person or by proxy shall be a quorum) and any such person may demand a poll.

The special rights or privileges attached to the Preference Shares will not be deemed to be varied, modified or abrogated by the creation or issue of further shares ranking *pari passu* therewith, or by the purchase or redemption by the Bank of its own shares.

Transfer of Shares

An instrument of transfer of a share which is in certificated form must be in writing in any usual form or other form approved by the directors of the Bank and must be executed by or on behalf of the transferor and (except in the case of fully-paid shares) by or on behalf of the transferee. The transferor will remain the holder of the shares transferred until the name of the transferee is entered in the register of members of the Bank in respect thereof.

The directors of the Bank may in the case of shares in certificated form, in their absolute discretion and without assigning any reason therefor, refuse to register any transfer of a share (not being a fully paid share) provided that, where any such shares are traded on the London Stock Exchange, such discretion may not be exercised in such a way as to prevent dealings in the shares of that class from taking place on an open and proper basis, and any transfer of a share on which the Bank has a lien. The directors of the Bank may also decline to register a transfer unless (i) the instrument of transfer is duly stamped (if so required), (ii) the transfer is in respect of only one class of shares and (iii) the transfer is in favour of not more than four persons as the transferee.

The Bank shares are in registered form. The registration of share transfers may be suspended at such times and for such periods as the directors may determine not exceeding 30 days in any year.

Notices or Other Documents

(a) Any notice or other document may be served by the Bank upon any holder of the Preference Shares, *inter alia*, personally, by sending it through the post in a prepaid envelope to such holder at its registered address, by leaving it at that address in accordance with Articles or by advertisement in one leading daily newspaper published in the United Kingdom and one leading English language daily newspaper and one leading Chinese language daily newspaper printed and circulated in Hong Kong. Holders who (having no registered address within the United Kingdom or Hong Kong) have not supplied to the Bank an address within the United Kingdom or Hong Kong for the service of notices shall not be entitled to receive notices from the Bank.

(b) Holders of the Preference Shares with a registered address or address for correspondence within the United Kingdom will have the right to have sent to them (at the same time as the same are sent to the holders of Ordinary Shares) all notices of general meetings of the Bank and a copy of every circular or other like document sent out by the Bank to the holders of Ordinary Shares.

TAXATION

General

Prospective investors should inform themselves as to the tax consequences within the countries of their residence and domicile of the acquisition, holding or disposal of Preferred Securities. The comments below are of a general nature based on law and published practice as at the date hereof in each jurisdiction referred to and do not constitute tax or legal advice and should be treated with appropriate caution. They relate only to the position of persons who are the absolute beneficial owners of their Preferred Securities and hold their Preferred Securities as an investment (unless otherwise specified). Any investors who are in doubt as to their personal tax position should consult their professional advisers. In assessing their tax position, investors should note that the Issuer is a Jersey limited partnership and not a legal entity separate from its partners.

Jersey Taxation

Investors in Preferred Securities (other than residents of Jersey) are not subject to any tax in Jersey in respect of the holding, exchange, sale or other disposal of the Preferred Securities. Distribution payments may be made by the Issuer without withholding or deduction for, or on account of, and without, any payment of Jersey income tax.

No stamp duties are payable in Jersey on the acquisition, ownership, exchange, sale or other disposal of Preferred Securities. Probate or letters of administration may be required to be obtained in Jersey on the death of a holder of a Preferred Security with an estate in Jersey, including Preferred Securities. Stamp duty is payable in Jersey on the registration of such probate or such letters of administration on the value of the deceased's estate in Jersey.

As a limited partnership, the Issuer is not itself a subject for assessment to Jersey income tax since it is not a legal entity separate from its partners.

On 3 June 2003, the European Union ("EU") Council of Economic and Finance Ministers adopted a directive on the taxation of savings income in the form of interest payments (Council Directive 2003/48/EC) (the "EU Savings Tax Directive"). It is proposed that, subject to a number of important conditions being met, each EU Member State will, from 1 January 2005, be required to provide to the tax authorities of another EU Member State details of payments of interest (or other similar income) paid by a person within its jurisdiction to or for the benefit of an individual resident in that other EU Member State; however, Austria, Belgium and Luxembourg will instead apply a withholding tax system for a transitional period in relation to such payments.

Jersey is not a member of the European Union and therefore is not required to implement the EU Savings Tax Directive. However, the Policy & Resources Committee of the States of Jersey has announced that, in keeping with Jersey's policy of constructive international engagement, Jersey, in line with steps proposed by other relevant third countries, proposes to introduce a withholding tax system in respect of payments of interest, or other similar income, made to an individual beneficial owner resident in an EU Member State by a paying agent situate in Jersey (the terms "beneficial owner" and "paying agent" for this purpose are as defined in the EU Savings Tax Directive). The withholding tax system would apply for a transitional period prior to the implementation of a system of automatic communication to EU Member States of information regarding such payments. During this transitional period, such an individual beneficial owner resident in an EU Member State will be entitled to request a paying agent not to withhold tax from such payments but instead to apply a system by which the details of such payments are communicated to the tax authorities of the EU Member State in which the beneficial owner is resident.

The States of Jersey has not yet adopted measures to implement these proposals but is expected to adopt such measures on the same timetable as EU Member States and other relevant third countries.

United Kingdom Taxation

In this section, the term "UK Investors" means persons who are resident (or in the case of individuals, ordinarily resident) in the United Kingdom for taxation purposes.

(a) Position of UK Investors

Classification of the Issuer

HSBC has been advised that the Issuer should be classified as a partnership for UK tax purposes. Accordingly, UK Investors in Preferred Securities should be subject to UK tax in respect of their investment in the Preferred Securities. UK Investors should be taxed on the basis that they are partners in the Issuer, and that the limited partnership interests are held on their behalf by the common depositary for Euroclear and Clearstream, Luxembourg as bare trustee. This treatment should, broadly, result in UK Investors being taxed as if they hold their proportionate share of the Issuer's assets. It is possible, however, that the Inland Revenue may seek to treat UK Investors in the Issuer as holding interests in a "unit trust scheme" and/or apply the "offshore fund" rules. This may have disadvantages for certain UK Investors. UK Investors who are in any doubt as to their tax position in respect of the Preferred Securities (or on exchange of Preferred Securities for Substitute Preference Shares) are strongly recommended to take independent professional advice.

(b) UK Withholding Tax on Distributions on the Preferred Securities

Payments of Distributions on the Preferred Securities may be made without withholding or deduction for or on account of UK tax.

(c) UK Withholding Tax on Interest on the Subordinated Note

The Subordinated Note issued by the Bank will constitute a "quoted Eurobond" provided it is and continues to be listed on a recognised stock exchange. The London Stock Exchange is a recognised stock exchange for these purposes. Accordingly, while the Subordinated Note is and continues to be a quoted Eurobond payments of interest on the Subordinated Note may be made without withholding or deduction for or on account of United Kingdom income tax.

(d) Stamp Duty and Stamp Duty Reserve Tax ("SDRT")

No UK stamp duty will be chargeable in respect of the issue of the Preferred Securities. Transfers of the Preferred Securities within a clearing system that has not made an election under section 97A Finance Act 1986 should not be chargeable to UK stamp duty unless such transfer is effected by means of a written instrument. Although a liability to UK stamp duty may arise on other transfers of, or agreements to transfer, Preferred Securities which are executed in the United Kingdom or which relate, wherever executed, to any property situate in, or to any matter or thing done or to be done in, the United Kingdom, it is not likely that any such duty will need to be paid in practice.

No liability to SDRT should arise in respect of the issue or subsequent transfer of the Preferred Securities.

No liability to UK stamp duty or SDRT will arise on issue of the Substitute Preference Shares unless they are issued either:

(i) to a clearing system (or to a nominee for a clearing system) and the clearing system has not made an election under section 97A of the Finance Act 1986; or

(ii) to a depositary (or to a nominee or agent for a depositary) who has issued or is to issue depositary receipts for the Substitute Preference Shares.

In either case, on issue of the Substitute Preference Shares there will be an SDRT entry charge at the rate of 1.5% of the value of the Substitute Preference Shares.

If the Substitute Preference Shares are issued to a clearing system (or to its nominee) which has not made an election under section 97A of the Finance Act 1986, there will be no SDRT on any subsequent agreement to transfer the Substitute Preference Shares and no stamp duty on any subsequent transfer of the Substitute Preference Shares so long as they are held in the clearing system and provided that any instrument of transfer or written agreement to transfer the Substitute Preference Shares is executed outside the UK and remains at all times outside the UK.

If the Substitute Preference Shares are issued to a clearing system (or to its nominee) which has made an election under section 97A of the Finance Act 1986, there will be no stamp duty or SDRT entry charge on the issue to the clearing system, but there will be a SDRT charge at the rate of 0.5% of the amount or value of the consideration on any subsequent agreement to transfer the Substitute Preference Shares so long as they are held in the clearing system. If the Substitute Preference Shares are held by a clearing system which has made a section 97A election and that election is subsequently terminated (whether at the instigation of the clearing system or the Inland Revenue or otherwise) an SDRT charge of 1.5% will arise as if, immediately after such termination, the Substitute Preference Shares had been transferred to a clearing system that had not made a section 97A election.

If the Substitute Preference Shares are issued to a depositary (or to its nominee or agent), there will be no SDRT on any subsequent agreement to transfer the depositary receipts representing interests in the Substitute Preference Shares and no stamp duty on any subsequent transfer of the depositary receipts provided that any instrument of transfer or written agreement to transfer the depositary receipts is executed outside the UK and remains at all times outside the UK.

SUBSCRIPTION AND SALE

Under a Subscription Agreement (the "Subscription Agreement") dated 31 October 2003 HSBC Bank plc, ABN AMRO Bank N.V., Citigroup Global Markets Limited, Credit Suisse First Boston (Europe) Limited, J.P. Morgan Securities Ltd and Merrill Lynch International (the "Managers") have agreed to subscribe for the Preferred Securities at a price of £1,000 per Preferred Security. The Managers will receive a combined selling, management and underwriting commission of £10 per Preferred Security and will be indemnified against certain liabilities by the Bank. The Managers are entitled to terminate the Subscription Agreement in certain circumstances before the issue of the Preferred Securities. The offering price and other selling terms may be changed at any time without notice.

United States of America

The Preferred Securities have not been and will not be registered under the Securities Act and may not be offered or sold within the United States or to, or for the account or benefit of, US persons. Terms used in this paragraph have the meanings given to them by Regulation S.

Each Manager has agreed that, except as permitted by the Subscription Agreement, it will not offer or sell the Preferred Securities, (a) as part of their distribution at any time or (b) otherwise, until 40 days after the later of the commencement of the offering and the issue date of the Preferred Securities, within the United States or to, or for the account or benefit of, US persons, and that it will have sent to each dealer to which it sells Preferred Securities during the distribution compliance period a confirmation or other notice setting forth the restrictions on offers and sales of the Preferred Securities within the United States or to, or for the account or benefit of, US persons.

In addition, until 40 days after commencement of the offering, an offer or sale of Preferred Securities within the United States by a dealer (whether or not participating in the offering) may violate the registration requirements of the Securities Act.

United Kingdom

Each Manager has further represented, warranted and agreed that:

(a) *No offer to public*: It has not offered or sold and will not offer or sell any Preferred Securities to persons in the United Kingdom prior to the expiry of a period of six months from the issue date of such Preferred Securities except to persons whose ordinary activities involve them in acquiring, holding, managing or disposing of investments (as principal or agent) for the purposes of their businesses or otherwise in circumstances which have not resulted and will not result in an offer to the public in the United Kingdom within the meaning of the Public Offers of Securities Regulations 1995;

(b) *Financial Promotion*: It has only communicated or caused to be communicated, and will only communicate or cause to be communicated, any invitation or inducement to engage in investment activity (within the meaning of section 21 of the Financial Services and Markets Act 2000 (the "FSMA")) received by it in connection with the issue or sale of any Preferred Securities in circumstances in which section 21(1) of the FSMA does not apply to the Issuer or the Bank;

(c) *General compliance*: It has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to any Preferred Securities in, from or otherwise involving the United Kingdom; and

(d) *Collective Investment Schemes*: It has only offered or sold and will only offer or sell Preferred Securities to (a) investment professionals falling within article 14(5) of the Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001 (the "Promotion of Collective Investment Schemes Order") and article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2001 (the "Financial Promotion Order"), who have professional experience of participating in unregulated schemes and matters relating to investments, or (b) persons falling within article 22(2) of the Promotion of Collective Investment Schemes Order and article 49(2) of the Financial Promotion Order.

General

No action has been or will be taken in any jurisdiction by the Issuer, the General Partner, the Bank or any Manager that would, or is intended to, permit a public offering of the Preferred Securities, or possession or distribution of this Offering Circular or any other offering material, in any country or jurisdiction where action for that purpose is required. Persons into whose hands this Offering Circular comes are required by the Issuer, the Bank and the Managers to comply with all applicable laws and regulations in each country or jurisdiction in which they purchase, offer, sell or deliver Preferred Securities or have in their possession, distribute or publish this Offering Circular or any other offering material relating to the Preferred Securities, in all cases at their own expense.

GENERAL INFORMATION

1. Application has been made to list the Preferred Securities on the Luxembourg Stock Exchange. In connection therewith, a legal notice relating to the issue of the Preferred Securities and the Partnership Agreement will be filed with the Register of Commerce and Companies in Luxembourg (*Registre de Commerce et des Sociétés à Luxembourg*), where the document may be examined and copies thereof may be obtained. The quotation on the Luxembourg Stock Exchange of the Preferred Securities will be expressed in pounds sterling as a percentage of the nominal amount per Preferred Security. For listing purposes, the Preferred Securities will be considered as debt securities. At the date hereof it is not intended to list the Preferred Securities on any other stock exchange.

2. The General Partner has obtained all necessary consents, approvals and authorisations in the United Kingdom and Jersey in connection with the issue of the Preferred Securities. The creation of the Preferred Securities was authorised by a resolution of the board of directors of the General Partner (acting in its capacity as general partner of, and on behalf of, the Issuer) on 30 October 2003. The issue of the Guarantee was authorised by resolutions of a committee of the Board of Directors of the Bank passed on 31 October 2003.

3. There has been no significant change in the financial or trading position of HSBC Bank Capital Funding (Sterling 1) L.P. and no material adverse change in the financial position or prospects of HSBC Bank Capital Funding (Sterling 1) L.P. since its establishment.

4. HSBC Bank Capital Funding (Sterling 1) L.P. is not, nor has been, involved in any legal or arbitration proceedings that may have, or have had since its establishment, a significant effect on the financial position of HSBC Bank Capital Funding (Sterling 1) L.P. nor is the General Partner aware that any such proceedings are pending or threatened.

5. There are no legal or arbitration proceedings against or affecting the Bank, or any of its subsidiaries or any of their respective assets, nor is the Bank aware of any pending or threatened proceedings, which are or might be material in the context of the issue of the Preferred Securities.

6. Save as disclosed in this document, there has been no significant change in the financial or trading position of the Bank or the Bank Group since 31 December 2002 and no material adverse change in the financial position or prospects of the Bank or the Bank Group since 31 December 2002.

7. The Preferred Securities have been accepted for clearance through Euroclear and Clearstream, Luxembourg. The following security codes have been assigned:

ISIN:	XS0179407910
Common Code:	017940791

8. Copies of the following documents will be available for inspection at (and, in the case of 8(c), 8(d) and 8(g) for collection (free of charge) from) the offices of the Listing Agent, Kredietbank S.A. Luxembourgeoise, and at the registered offices of the Bank, the Issuer and of the Paying Agents whose addresses are shown elsewhere in this Offering Circular during normal business hours for so long as the Preferred Securities are outstanding:

   (a) the Partnership Agreement (which includes the form of the Global Certificate);

   (b) the memorandum and articles of association of the Bank;

   (c) the audited financial statements of the Bank for the years ended 31 December 2000, 31 December 2001 and 31 December 2002;

   (d) the consents and authorisations referred to in paragraph 2 above;

   (e) the Guarantee;

   (f) the Subscription Agreement; and

   (g) a copy of this Offering Circular together with any supplemental offering circular.

For so long as the Preferred Securities are listed on the Luxembourg Stock Exchange, the most recently published audited annual financial statements and consolidated unaudited semi-annual financial statements of the Bank, and the most recently published audited annual accounts of the Issuer, will also be available at the offices of Kredietbank S.A. Luxembourgeoise in Luxembourg. The Bank does not publish non-consolidated interim financial statements and the Bank did not publish interim financial statements as at 30 June 2003. The first annual accounts of the Issuer are expected to be prepared for the period commencing on 31 October 2003 and ending on 31 December 2003. The Issuer will not publish semi-annual interim accounts.

9. The financial information relating to the Bank Group contained in this Offering Circular does constitute statutory accounts within the meaning of Section 240(5) of the Companies Act 1985. KPMG Audit Plc, Chartered Accountants and Registered Auditor of 1 Canada Square, London E14 5AG, have been auditors to the Bank for the financial years ended 31 December 2000, 2001 and 2002. The auditors have issued unqualified reports in respect of the Bank's financial statements for the financial years ended 31 December 2000, 2001 and 2002, without any statements under Section 237(2) or (3) of the UK Companies Act 1985 and statutory accounts for the financial years ended 31 December 2000, 2001 and 2002 have been delivered to the Registrar of Companies.

10. No redemption of the Preferred Securities (optional or otherwise) and no purchase and cancellation of the Preferred Securities will be made by the Issuer, the General Partner or the Bank without such prior consent of the FSA as may for the time being be required. These requirements and restrictions do not affect the ability of the Bank's subsidiaries and affiliates to engage in market-making activities in relation to the Preferred Securities.

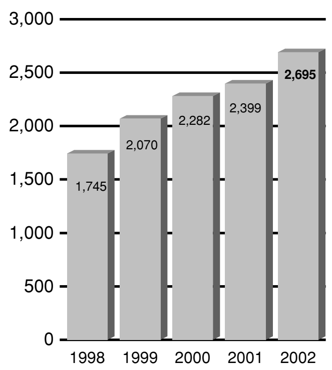
ANNEX A
HSBC BANK PLC
ANNUAL REPORT AND ACCOUNTS 2002

Annual Report and Accounts 2002

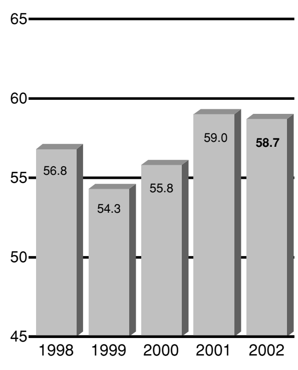
Financial Highlights

	2002	2001 *	2000 *	1999 *	1998 *
For the year (£m)					
Operating profit before provisions	**2,695**	2,399	2,282	2,070	1,745
Profit on ordinary activities before tax	**2,285**	2,290	2,046	1,724	1,522
Profit attributable	**1,379**	1,470	1,386	1,201	1,042
At year-end (£m)					
Shareholders' funds	**16,455**	15,648	14,873	5,016	4,780
Capital resources	**12,768**	12,209	11,527	8,121	7,918
Customer accounts and deposits by banks	**155,234**	147,665	131,329	77,874	72,181
Total assets	**218,378**	202,309	185,426	106,468	104,846
Ratios (%)					
Return on average shareholders' funds (equity)	**8.5**	9.3	18.7	25.9	23.4
Capital ratios					
— total capital	**10.3**	10.7	10.7	11.3	11.1
— tier 1 capital	**7.1**	6.8	6.5	6.8	6.8
Cost:income ratio (excluding the amortisation of goodwill)	**58.7**	59.0	55.8	54.3	56.8

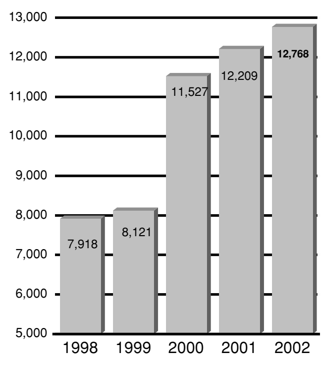
Operating profit before provisions (£m)



Cost:income ratio (%)



Capital resources (£m)



The financial highlights are influenced by changes in the group structure over the five years. The most significant acquisitions are as follows: in 2000, HSBC Private Banking Holdings (Suisse) SA, CCF S.A. (formerly Crédit Commercial de France S.A.); in 2001, HSBC Investment Bank Asia Limited, Banque Hervet, Demirbank TAS, HSBC Guyerzeller Bank AG; in 2002, HSBC Trinkaus & Burkhardt KGaA, HSBC Republic Bank (UK) Limited and activities of HSBC Investment Bank plc.

* *Figures for 2001 and 2000 have been restated to reflect the adoption of Financial Reporting Standard 19, 'Deferred Tax', details of which are set out in Note 1(d) on the Accounts on page 64. Apart from shareholders' funds at 1999 year-end, the 1999 and 1998 comparatives have not been restated as it is considered that any adjustments made would not significantly alter the figures. Therefore, any benefit to be obtained from restatement would be outweighed by the cost of the exercise.*

Annual Report and Accounts 2002

Contents

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING COMMENTS

This document contains certain forward-looking statements with respect to the financial condition, results of operations and business of HSBC Bank plc (the 'bank') and its subsidiary undertakings, joint ventures and associates (together the 'group'). Among other sections, 'Business Description' and 'Financial Review' contain various forward-looking statements which represent the bank's expectations or beliefs concerning future events and involve known and unknown risks and uncertainty that could cause actual results, performance or events to differ materially from those expressed or implied in such statements. Certain statements, such as those that include the words 'potential', 'value at risk', 'estimation', 'hypothetical', and similar expressions or variations on such expressions may be considered 'forward-looking statements'. Other factors that could cause actual results, performance or events to differ materially from those expressed or implied in this document include, but are not limited to, general economic conditions, changes in competition, and fiscal and other government policies adopted in the UK and in other countries in which the group has significant business activity or investments.

Presentation of Information

This document comprises the *Annual Report and Accounts 2002* for HSBC Bank plc (the 'bank') and its subsidiary undertakings, joint ventures and associates (together the 'group'). It contains the Directors' Reports and Accounts, together with the Auditors' Report, as required by the UK Companies Act 1985.

The bank's obligation to file annual reports with the US Securities and Exchange Commission has been suspended following, among other things, the re-listing of two issues of the bank's subordinated notes to London from New York. As a consequence, an *Annual Report on Form 20-F* for 2002 has not been prepared.

Business Description

Introduction

HSBC Bank plc and its subsidiaries form a UK-based financial services group providing a wide range of banking, treasury and financial services to personal, commercial and corporate customers, mainly in the United Kingdom and continental Europe. The bank's strategy is to build long-term relationships and reward customers through value-for-money products and high-quality service.

HSBC Bank plc (formerly Midland Bank plc) was formed in England in 1836 and subsequently registered as a limited company in 1880. In 1923, the company adopted the name of Midland Bank Limited which it held until 1982 when the name was changed to Midland Bank plc.

During the year ended 31 December 1992, Midland Bank plc became a wholly owned subsidiary undertaking of HSBC Holdings plc ('HSBC Holdings'), whose Group Head Office is at 8 Canada Square, London E14 5HQ. HSBC Bank plc adopted its current name, changing from Midland Bank plc, in the year ended 31 December 1999.

HSBC Holdings, together with its subsidiary undertakings, joint ventures and associates, is referred to as the 'HSBC Group'. The HSBC Group is one of the largest banking and financial services organisations in the world, with over 8,000 offices in 80 countries and territories in Europe, the Asia-Pacific region, the Americas, the Middle East and Africa. Its total assets at 31 December 2002 were £471 billion. The bank is the HSBC Group's principal operating subsidiary undertaking in Europe.

Since 1999, the group has been following the HSBC Group's 'Managing for Value' strategy, which focuses on the delivery of wealth management services to personal customers, aligning its corporate and investment banking businesses, and growing its commercial business. As part of the HSBC Group's key initiative to align corporate and investment banking, the activities of HSBC Investment Bank plc were transferred to the bank in November 2002.

As at 31 December 2002, the bank's principal subsidiary undertakings and their main geographical areas of activity were:

CCF S.A. (formerly Crédit Commercial de France S.A.)	France
HSBC Asset Finance (UK) Limited	United Kingdom
HSBC Bank A.S.	Turkey
HSBC Bank International Limited	Jersey
HSBC Bank Malta p.l.c.	Malta
HSBC Guyerzeller Bank AG	Switzerland
HSBC Invoice Finance (UK) Limited	United Kingdom
HSBC Life (UK) Limited	United Kingdom
HSBC Rail (UK) Limited	United Kingdom
HSBC Republic Bank (Guernsey) Limited	Guernsey
HSBC Republic Bank (Suisse) SA	Switzerland
HSBC Republic Bank (UK) Limited	United Kingdom
HSBC Trinkaus & Burkhardt KGaA	Germany
HSBC Trust Company (UK) Limited	United Kingdom

On 28 June 2002, Merrill Lynch HSBC Holdings Limited ('MLHSBC') became a 100 per cent owned subsidiary of the HSBC Group. On 1 November 2002, Merrill Lynch HSBC Limited was transferred to the bank. MLHSBC was formed as a 50:50 joint venture between the HSBC Group and Merrill Lynch in April 2000 to provide direct investment and banking services, primarily over the internet, to 'mass affluent' investors outside the United States. MLHSBC has a licence to continue to use Merrill Lynch as part of its name and for clients to have access to Merrill Lynch research for up to two and a half years from 28 June 2002.

On 1 July 2002, the group acquired a 73.47 per cent interest in HSBC Trinkaus & Burkhardt KGaA, as part of the HSBC Group's strategic restructuring to align its corporate and investment banking activities.

On 1 July 2002, the group acquired 97.82 per cent of HSBC Republic Bank (UK) Limited, as part of the HSBC Group's continued restructuring of its Private Banking activities.

On 19 September 2002, HSBC Bank A.S. in Turkey purchased 100 per cent of Benkar Tuketici Finansmani ve Kart Hizmetleri A.S. ('Benkar') a consumer finance and card services company, from Boyner Holding A.S.

On 30 November 2002, the investment banking activities of HSBC Investment Bank plc were transferred to the bank.

The bank's strategy centres on building long-term customer relationships by listening to customers, understanding their needs and delivering the most effective solutions. In accordance with this strategy, the bank continues to invest in improving customer relationship management systems, creating more convenient channels, developing innovative and flexible products and building a reputation for fair pricing.

In line with the HSBC Group, the bank commenced a communication programme in the UK during 2002, designed to give the HSBC brand a strongly differentiated image in the minds of customers, with the ultimate aim of increasing business. The results at the end of 2002 were encouraging, with a marked improvement in the level of awareness of the HSBC brand.

While the bank continues to develop telephone and internet propositions, it remains committed to community banking and its most important delivery channel, the branch network where it has 1,633 branches, including 42 outlets in supermarkets. Experienced managers are located in local branches with authority to provide a timely, efficient and flexible service to both personal and business customers. Developments in the branch network continue to focus on creating more time for branch staff to serve customers by removing back office work to central processing sites.

The bank has an extensive network of cash, pay-in and statement machines and provides some 3,000 Automated Teller Machines (ATMs) for use by customers. Customers also have access to over 42,000 cash machines through the UK LINK network and over 835,000 ATMs worldwide.

Global processing, through the establishment of Group Service Centres (GSCs), continues to play an important role in the HSBC Group's strategic aim of pursuing economies of scale in order to increase productivity and achieve a competitive and economic advantage. Since their introduction in 1996, the GSCs have progressively fulfilled more of the back office functions previously undertaken by the HSBC Group's principal members across the world, in the UK, the Hong Kong SAR, the UAE, the United States and Canada. The centres provide a wide range of activities for a growing number of business areas, including cards, mortgage processing, investment products and retail banking.

The bank continues to seek synergies to maximise long-term value. Two outsourcing projects have now been completed: cash processing to Securitas Cash Management Limited and cheque and credit clearing services to Intelligent Processing Solutions Limited. The bank works closely with its new partners to improve processes and systems for the benefit of customers, as well as increasing efficiency.

The role of HSBC Bank and its staff in the community

The group's 76,500 employees are the key to its success both in providing high quality customer service and in making HSBC Bank plc 'The world's local bank'.

The bank is proud of its record in community activities and is committed to supporting education and the environment, particularly projects focusing on business, finance and languages for disadvantaged children. A key part of the community support programme is the involvement of staff in activities such as the Young Enterprise programme, where staff participate as volunteer advisers to students. Staff are also very active in fund-raising activities including the annual BBC Children in Need appeal. In 2002, over £600,000 was raised in support of this appeal. The bank is one of the three key principal sponsors. In addition, sponsored walks and charity runs raised £136,000 for the mobility charity Whizz-Kidz and £145,000 for the Cancer Research UK's Race for Life.

HSBC Bank plc staff also take part in the HSBC Group's 'Investing in Nature' programme. This is a partnership with the World Wildlife Fund (WWF), Botanic Gardens Conservation International and Earthwatch, under which £31 million will be donated to fund conservation projects worldwide. Staff also work on vital conservation research projects worldwide.

The bank has introduced an Environmental Management System following Department for the Environment, Food and Rural Affairs' guidelines and set internal performance targets for emissions from energy and business travel, consumption of water, and management of waste. The bank is actively seeking ways to minimise its impact on the environment, e.g. centralisation of waste collection.

Business Description (continued)

Business Segments

The bank divides its activities into the following business segments: UK Personal Banking, UK Commercial Banking, UK Corporate and Institutional Banking, and UK Treasury and Capital Markets; Investment Banking; International Banking; CCF; Private Banking (formerly HSBC Republic); and HSBC Trinkaus & Burkhardt.

UK Personal Banking

The bank's personal banking activities comprise current accounts, savings, personal lending, mortgages, cards and wealth management services. These are delivered to customers through a number of channels under the HSBC and First Direct brands.

The personal banking market has seen further growth by 'direct' (especially internet) providers and aggressive pricing competition by mortgage-based banks. The bank continues its strategy to broaden and deepen its personal customer relationships. In surveys, 93 per cent of the bank's personal customers state they were satisfied or very satisfied with the service they received. In a survey completed in December 2002, the percentage of customers saying that they were very satisfied was 52 per cent, while the average for the main competitors, Barclays, Lloyds TSB, NatWest, Halifax and Abbey National, was 47 per cent.

Customer demand for remote services continued to grow and the bank responded with further investment in internet banking, TV banking and self-service machines. Some 1.2 million customers are now registered for personal internet banking (www.hsbc.co.uk) with a further 177,000 customers registered for TV banking. These customers access their bank account details around one million times weekly via personal internet banking and TV banking and over 50 per cent of the payments on demand are being made online.

The number of quality screen-based 'Individual Solutions' sales contacts increased to over nine million. 'Individual Solutions' accounted for 33 per cent of all customer contacts in 2002.

The number of individual service reviews or face-to-face discussions with customers increased from 234,000 in 2001 to 485,000 in 2002.

Customers continue to seek easy access to banking services and five million calls per month are now answered across the HSBC group call centres (excluding First Direct). Over 50 per cent of all calls to the telephone banking service are handled through the automated interactive voice recognition system, providing an efficient service for the customer and cost-effective delivery for the bank.

In response to growth in call volumes 200,000 calls per month are now answered in a call centre in Hyderabad, in India, leveraging the bank's international infrastructure. Customers' desire to buy financial products and services over the telephone continues to grow. Over 780,000 sales were made by Direct Financial Services in 2002, an increase of over 57 per cent on 2001. More than £740 million was advanced on personal loans agreed by the centralised telephone operation. Automated dialler technology has been employed to increase the efficiency of outbound telephone contacts.

The bank introduced 'intelligent' call routing to direct callers, using the automated telephone banking service, to a customer service representative when it may be of benefit to the customer.

The Customer Relationship Management ('CRM') system, developed in recent years, has been further enhanced. Regarded as class-leading among UK financial institutions, this system makes relevant customer information available to all customer-facing staff and facilitates highly personalised marketing. The CRM system now helps offer tailored solutions to internet banking customers.

A new service, 'Your Personal Financial Summary', was introduced providing over six million personal customers with a single document summarising all their products and services with the bank. It has also led directly to an additional 216,000 contact opportunities, through customer requests for products and services.

Current accounts — the bank's research shows that four out of five customers move their accounts for reasons other than price. In 2002, the bank increased its current account base by 3.9 per cent. The bank operates a very effective account switching service that comfortably meets the recommendations made by the Banking Services Consumer Codes Review Group. In 2002, HSBC Bank plc was the first major bank to significantly reduce overdraft interest rates for unauthorised borrowing. The bank has chosen to improve overdraft pricing as customer research suggests it is what most customers would like to see changed.

The HSBC *Premier* customer base grew by 44 per cent compared with 2001 and these customers have an average of over five bank products. The *Premier* telephone service now enables the opening of personal loans, credit cards and savings accounts. Twenty-two per cent of *Premier* customers are registered for personal internet banking. HSBC *Premier* International Services was launched during the year to meet the needs of customers who require financial services in more than one country.

Savings — the bank offers an extensive range of savings accounts including Individual Savings Accounts (ISAs), high interest savings (60-day notice), instant access savings and young savers accounts. Average balances increased by 19 per cent over the last year and by 51 per cent over the last two years. According to a *MORI* report in June 2002, the bank was a top five provider of cash ISAs in the UK.

Personal lending — the bank has outperformed the market in personal loan volumes, achieved through enhanced customer contact programmes. Market share increased from 5.2 per cent in 2001 to 6.3 per cent in 2002 without sacrificing credit quality. More than 127,000 personal loans were arranged by telephone or over the internet.

Mortgages — in 2002, the bank advanced over 130,000 mortgages, twice as many as in 1999 before the introduction of the bank's 'new deal for customers'. The bank's market share of net new lending increased from 2.5 per cent in 1999 to nearly 5.8 per cent in 2002 and total mortgage balances nearly doubled in the last five years. The bank was again the winner of the *What Mortgage?* award for Best National Bank over two, five and 10 years and the *Your Mortgage* magazine winner for the first time with the Editor's Special Award for its price promise. A 'Buy to Let' mortgage was launched in May 2002.

Cards — the bank issues a comprehensive range of credit cards under the Mastercard and Visa brand labels and develops high value customer relationships by providing tailored credit cards as an integral part of the bank's customer relationship strategy. Thirty per cent of new customers are now offered premium cards. The HSBC *Premier* credit card has one of the best interest rates in the market with no annual fee.

The bank continues to work closely within the industry to counter card fraud. During 2002, the bank rolled out more cards, incorporating smart card technology and has contained its costs of card fraud below industry averages.

Wealth management — this includes pensions, loan protection, investments, general insurance, private client services, estate planning, executorships and stockbroking activities.

The bank's combined market share for its principal investment products, Open Ended Investment Companies and ISAs, was maintained at over 5 per cent during 2002.

Net sales to personal customers of the bank's life, protection and investment products (through its tied sales force) were 7 per cent higher than 2001, despite a difficult investment market. The bank is well placed to grow wealth management business as a result of 'depolarisation', a series of changes to the regulations governing the way investment and protection products are distributed that will allow the bank to supply third party products as well as its own. The bank's strategy will be to give customers more choice.

The cross-sales opportunities arising from increased mortgage sales have resulted in an increased market share for mortgage term life policies, from 5.4 per cent in the final quarter of 2001 to 5.8 per cent in the third quarter of 2002. Market share for all individual regular premium life insurance policies has increased from 3.8 per cent in the final quarter of 2001 to 4.7 per cent in the third quarter of 2002. The bank is one of the leading providers of individual income protection policies with market share increasing strongly from 14.5 per cent in the final quarter of 2001 to 19.3 per cent in the third quarter of 2002. The Individual Income Protection Plan was awarded a 'best buy' in *Which?* magazine in 2002.

Private client services offer discretionary portfolio management services and independent financial advice to high net worth individuals. Despite the impact of adverse stock markets, new funds increased by 8 per cent over 2001. Over the last three years, the bank has increased new funds by 59 per cent and increased sales of broked insurance and investment products by over 80 per cent. HSBC Trust Company (UK) Limited was ranked second in a survey of the top 50 independent financial advisers by *Investment Advisor* magazine.

The bank launched two new general insurance products in 2002: 'Home Emergency' and 'Legal Assistance'. For the second year running 'Home Cover' received *Which?* 'best buy' recommendations for both buildings and contents cover.

Business Description (continued)

Merrill Lynch HSBC Limited has now been integrated into the personal banking business, providing banking and investment services to self-directed investors, who can transact through its web site (www.mlhsbc.com) or client contact centres.

First Direct — provides personal 24-hour banking, mortgage and wealth management services, 365 days a year by telephone and the internet.

First Direct's pre-tax profit increased by 51 per cent in 2002 to £49.5 million as a result of strong customer demand, increased use of the internet and product innovation. It has maintained its lead as the UK's most recommended bank according to *MORI*.

Asset balances grew by 35 per cent during the year, predominantly due to the launch of the 'smartmortgage' product in July 2001. Mortgage balances grew from £1.6 billion in June 2001 to £3.6 billion by the end of 2002.

The launch of the Bonus Savings Account in October 2002 has attracted balances of over £1.3 billion to date, contributing to a 23 per cent growth in customer deposit balances during the year.

First Direct attracted 88,900 new customers during 2002. It remains Britain's most recommended bank having consistently the most satisfied banking customers in Britain. Only 5 per cent of customers recorded a complaint in the last year, lower than any other bank, and 74 per cent were very satisfied with the way the complaint was handled, considerably ahead of any other bank. First Direct customers hold an average of 2.93 products each, more than any other UK bank.

First Direct continues to win awards. During 2002, these included the top ranking for 'understanding customer needs' by *Reader's Digest*, providing 'best customer service' by *Personal Finance* magazine, 'best current account provider' awarded by *Guardian Observer Consumer Finance* and 'best direct sharedealing service' by *Your Money Direct*. First Direct also received awards from *What Mortgage* magazine for 'Best Overall National Lender over 10 years' for the fourth successive year and for 'Best Centralised Lender over 10 years' for the ninth successive year. In addition, First Direct was recognised as being in the 'Top 100 Companies to work for' in a report issued by the *Sunday Times*.

First Direct continued to grow its independent life, pensions and investments business, offering products from leading providers, coupled with a telephone-based advice service. Commission income in 2002 was 30 per cent higher than in 2001.

The growth in First Direct's e-channel services has continued with 54 per cent of customers now using the internet (www.firstdirect.com), mobile phone or WAP banking. Sixty per cent of customer contacts with First Direct are now made electronically. Sales from internet banking and mobile phone banking sources have increased, with 12 per cent of all product sales now attributable to e-channels.

UK Commercial Banking

The bank's commercial banking business focuses on providing products and services to a broad range of commercial organisations, from sole proprietors to major companies. The bank remains committed to serving local business communities through its extensive network of branches. This commitment was further strengthened in January 2002, when a number of specialist sales forces were integrated into the branch network. Working with relationship managers, this facilitates a 'one-stop shop' for business financial services.

The bank is also committed to increasing customer choice and, during 2002, invested in the development of alternative sales channels. Dedicated business telephone banking centres have been set up in Swansea, Edinburgh and Hyderabad in India and handled inbound calls from approximately 134,000 registered users in 2002. A business outbound telephone centre was established in Leicester during 2002 and made over 38,000 referrals to branches and product managers, 60 per cent of which resulted in a sale.

In January 2002, the bank launched 'Business Internet Banking' (www.bib.hsbc.com). This service extends electronic banking to the bank's smaller business customers and 35,000 customers registered in its first full year of operation. Significant growth in this channel is anticipated in 2003, once active marketing commences.

HSBC Bank plc has recently been named 'Best High Street Clearing Bank for Small Businesses' in the prestigious biennial survey of their membership undertaken by the Forum of Private Business (FPB). Their survey of over 6,500 members ranked the bank the best of the major banks in terms of customer satisfaction, competence of managers and friendliness of staff, least cause to complain, speed of service, closeness of relationship to customers and fairness of bank charges.

In a separate survey, the UK 200 Group, the country's largest national group of accountancy firms, also voted HSBC Bank plc the 'Best Bank for Business' for the third year running.

The members of Factors Chain International ('FCI') voted the bank the 'Best Factor in the UK'. FCI is a chain of correspondent debt factors who offer export services in countries where the exporting factor has no representation. Each member of FCI is able to vote on the service it receives from correspondents.

By focusing on customer needs, employing product specialists, investing in new sales channels and effective marketing, the bank has increased its share of the business start-up market and seen a strong net increase in customers switching between banks. During 2002, over 87,000 start-up accounts were opened, an increase of more than one third over 2001. The number of customers moving accounts from competitors to the bank has also grown, contributing to an increase in the customer base of more than 6 per cent.

The year has also seen a good performance on customer retention. Attrition levels for the bank's customer base are well below those of its peers, due to the quality of service and the effective delivery of relationship management. This is supported by the FPB survey referred to above, which showed the bank to have the lowest proportion of customers who considered switching banks.

During the year, discussions took place with the Office of Fair Trading (OFT) following the completion of the Competition Commission's report on the provision of banking services to small and medium-sized businesses. The bank has developed a package of initiatives estimated to be worth £80 million per annum to its customers. With effect from 1 January 2003, interest on current accounts is paid automatically to all qualifying customers. Further initiatives include the introduction of a new instant access savings account and better terms for start-up businesses. In its report, the Competition Commission placed HSBC Bank plc ahead of its high street competitors. Their survey showed that the bank's customers are the most satisfied with their bank overall, the bank is top-ranked for both business account services and relationship management, and the bank's customers are the most satisfied with pricing.

Payments and cash management — the bank provides a full range of account services to small and medium market commercial banking customers including the payment of supplier invoices, staff-related expenses and the collection of customers' receivables. Core services are cheque and cash processing, money transmission and electronic payments designed to meet all domestic and international needs. Customers can access these services via a full range of channels including branch, telephone, internet or other electronic services. The bank is one of the largest users of both BACS and CHAPS payment systems and is fully involved in all updates and enhancements. The bank promotes cross-border solutions to its growing commercial customer base with pan-European needs, utilising the group's presence in Europe, in particular CCF in France and HSBC Trinkaus & Burkhardt in Germany.

Business current and deposit accounts — the bank offers an extensive range of business current and deposit accounts. Deposit balances increased by 9 per cent on 2001, influenced by a widespread movement away from equity investments during the year. Products and services are reviewed regularly to ensure they reflect changing market requirements and, accordingly, the 'Business Money Manager' account will be launched in 2003 as the bank's primary commercial savings product. This account has the flexibility of a sight deposit and also rewards the customer for the length of time money is deposited.

Trade services — with experience going back 138 years, trade services are a core strength of the HSBC Group. A strong presence in Europe, Asia-Pacific, the Americas and the Middle East has resulted in the HSBC Group being recognised as one of the world's largest trade services organisations. In this context, the bank offers a range of services and expert advice to both experienced importers and exporters, and those considering trading internationally for the first time. The HSBC Group's local knowledge and international expertise help to simplify the processes and reduce the risks associated with trading overseas.

Following the recent weakness in the global economy, it is now more important than ever for customers to seek the type of tailored trading solutions afforded by the bank's blend of traditional and specialised products. As well as helping with the terms of trade, the bank can finance international business, offer foreign exchange facilities, establish guarantees and make and receive payments on behalf of customers. The bank has successfully implemented an internet-based documentary credit advisory service and will continue to look at ways of utilising modern technology. The bank acquired an export services business in 2002 and now offers a complete range of export administrative services covering document preparation, data provision, freight and credit management.

Despite the weakness of international trade, especially exports, customer numbers increased 5 per cent in 2002, resulting in a significant increase in new business over the previous year.

Lending — business lending remains a core activity for the bank. A range of specialist products such as invoice finance, leasing, and hire purchase complement overdrafts and term loans. Medium-term lending grew by 9.3 per cent during the year, driven by a customer-focused approach to structured lending and improved pricing tools. However, the bank continues to adopt a prudent credit management policy.

HSBC Vehicle Finance is one of the UK's largest providers of contract hire to businesses. It offers a range of propositions to meet customer needs for the acquisition and management of vehicles across all customer segments: personal, commercial and corporate fleet customers. Total fleet size has grown to 79,000 vehicles and volumes of new business acquired from bank relationships are up 22 per cent, reflecting the benefits of integration with the branch network.

The 'HSBC DriverQuote' product, an online fleet contract hire quotation system, was launched during the year. The system is a market leader in its field and, as a result, won 'The Fleet Innovation Gold Award' by the fleet and business car magazine *Fleet Week*.

In 2002, there was significant growth within invoice finance, 10 per cent in the client base and 3 per cent in client invoices factored. This included a 13 per cent growth in the number of clients taking the credit protection product and supports the 11 per cent income growth seen by the business. Recognising the impact of a deteriorating economic environment, particularly for manufacturing, this represents significant underlying growth in the business. Integration of the sales force within the network continues to improve introductions and new business income grew by 25 per cent in the year.

Business wealth management — the bank offers a wide range of expertise to help business owners and directors manage their business and personal wealth efficiently through to retirement. For business protection, the bank offers products such as key person insurance and partnership protection. Sales of products such as these have grown significantly, up by 11 per cent on 2001. The bank is now one of the top providers of regular premium stakeholder pensions in the UK market, with a 6.3 per cent market share. Investment income has performed well, despite the performance of equities during the year.

Corporate, Investment Banking and Markets

The HSBC Group is ideally placed to serve the international operations of its corporate and institutional clients, whose needs are increasingly complex. The bank is committed to tailoring its services to meet the demands of these large clients where it already has a very strong position, enjoying relationships with many of the FTSE 250 corporates and financial institutions. Consequently, resources have been organised to support a pan-European proposition within the global context, to meet the needs of multi-banked clients who want to concentrate their relationships with a smaller number of core global banks.

Building on its capability here, the group has integrated its wholesale banking activities bringing together the corporate, treasury and investment banking skills required to service these important clients.

UK Corporate and Institutional Banking (CIB)

The bank's UK corporate and institutional banking team comprises over 100 relationship managers, based in London, providing dedicated relationship management to corporate and financial institutional clients.

These relationship managers are organised into pan-European specialist industry groups to enable the group to better understand and respond to the needs of customers, providing 'one-stop shop' sourcing of a wide range of products and services from across the HSBC Group. In this way, the bank has been able to support clients seeking to develop globally and needing a range of different financial services. These services include products offered by the bank's Treasury and Capital Markets division, details of which are shown on pages 11 and 12.

Payments and cash management — the HSBC Group is a major provider of global payments and cash management services.

Amongst major corporates, the bank is recognised as a leading supplier of domestic and international money transmission and payments services. The *Euromoney* 2002 survey reported the bank as being one of the top three international cash management providers.

The bank continues to extend comprehensive and global cash management solutions to corporate and institutional clients across Europe. Further investment in its European infrastructure complements investments by the HSBC Group in other regions of the world, and makes the HSBC Group one of the few international banks able to offer cash management solutions on a worldwide basis.

Electronic banking channels continue to be developed and enhanced, including the extension in 2002 of direct bank-to-customer connectivity. In 2003, a dedicated internet banking capability for corporate and institutional clients will be launched.

In the financial institutions sector, the bank is the leading CHAPS bank and a recognised leader in payment services across a range of currencies. The bank's treasury clearing proposition has been enhanced by the launch of Continuous Linked Settlement services in September 2002. The bank took a lead position in this banking industry initiative and is actively using the system to launch new service propositions to institutional and corporate customers and reduce its own risk.

Global investor services ('GIS') — offers comprehensive international, European and UK custodian services and operates in 70 markets worldwide. GIS has over 1,400 contracted customers from the investment industry, with over £700 billion of assets under custody.

On this platform, GIS also engages in agency stocklending of both fixed income and equity instruments and offers corporate trust services worldwide for the issuing and paying of debt instruments. The strength in such value-added services has seen GIS well positioned to withstand the difficult trading conditions experienced in the investment markets in 2002.

GIS also maintains a key role in the HSBC Group's wealth management strategy, acting as custodian to both HSBC Asset Management and the HSBC Group's private client business. GIS has invested heavily in developing the HSBC Group's new core custody system, which is due to be implemented in 2005.

Global funds services — provides a wide range of investment administration and performance consultancy services for owners and managers of investment funds with over 80 now using them since their launch in 2000. The investment administration includes daily processing and pricing for both onshore and offshore funds. Performance consultancy covers both relative fund performance analysis and Global Investment Performance Standards verification.

Lending — this continues to be a core product for the corporate market and the bank's client-focused approach allows it to deliver the most appropriate lending product to meet the needs of these international clients. This may be vanilla overdraft or term debt although, increasingly, much business is done through the bank's debt capital markets team where the bank is ranked first in bond issuance in all currencies for UK and French corporations.

A wide range of specialist products is also provided, which meet the short-, medium- and long-term financing requirements of clients. The bank's prudent credit management policy, together with its industry specialist relationship approach has enabled it to better support clients and strengthen relationships in difficult market conditions.

Structured finance — provides a selection of finance and operating lease products to support corporate clients' investment in large-scale, long-term assets. The business is primarily focused on clients in the transport and industrial sectors, with the bulk of the assets financed being railway rolling stock, passenger aircraft, cargo shipping and industrial plant.

UK Treasury and Capital Markets

The bank's major dealing room in London serves as the hub for the HSBC Group's European network of treasury and capital markets activities. It delivers a high-quality tailored service to the HSBC Group's corporate, commercial and institutional clients. The major product areas are money markets, foreign exchange and fixed income. These are complemented by activities in exchange-traded futures, precious metals and banknotes.

Money markets — this business is a conduit for personal and corporate deposits in all principal currencies. The bank is a major participant in the professional money markets, taking institutional deposits and managing the bank's retail bank clearing operations. In the past two years, the bank has reduced its reliance on the interbank market for the application of surplus liquidity, with the

Business Description (continued)

establishment of a highly rated corporate bond portfolio, which now stands at £4.9 billion.

Foreign exchange (FX) and foreign exchange derivative markets — the HSBC Group is a leading participant in the global foreign exchange markets and continues to rank highly in a number of international polls. The bank provides its customers with sophisticated, round-the-clock coverage in all of the world's major currencies. Moreover, the extensive geographical reach of the HSBC Group enables the bank to provide its customers with detailed knowledge and support in less liquid and emerging markets to cater for their execution and hedging needs.

FXall, of which the HSBC Group is a founder member, has re-affirmed its position as the leading multi-contributor FX e-trading platform, winning awards in *Euromoney* and *FXWeek* in 2002. The HSBC Group has also launched www.markets.hsbc.com which was recently voted number one 'single bank internet trading site for FX' by the corporate survey in *FX Week*'s annual poll. There has been significant growth in these distribution channels over the past year, with 15 per cent of the bank's customer FX activity now executed electronically.

Fixed income — this area includes the HSBC Group's debt capital markets and interest rate derivative activities. The HSBC Group is a leading originator and underwriter, having particular strengths in sterling, euros, and Hong Kong dollars. It serves a diverse customer base: sovereign governments and agencies, supranational agencies, financial institutions and major corporations. Specialised capital market solutions are provided for project and asset-backed financing. In the secondary markets, the HSBC Group is a major market maker, both in the government and non-government bond markets. Risk management advisory services are provided to assist clients in managing their interest rate and currency risks through the use of derivative products. The pan-European debt platform created with the acquisition of CCF is now bringing rewards in debt origination and bond issuance.

The importance of electronic platforms continues to grow in the fixed income arena, with new e-channels in support of debt origination activities. During 2003, it is intended to launch an e-syndications book building application across the HSBC Group and to selected clients. Secondary market activities are aided by giving clients access to the multi-dealer TradeWeb platform.

Exchange-traded futures and options — Treasury and Capital Markets offers an international execution, research and clearing service for key currency, interest rate, bond and equity futures and options, with innovative and flexible account structures and a sophisticated online interface.

Investment Banking

There are three main components of investment banking:

Corporate finance and equities — this business provides corporate and institutional clients with advisory services in connection with mergers and acquisitions, asset disposal, equity capital, stock market listings, privatisation and capital restructuring. The equity business focuses on the core sectors relevant to the group's clients offering a wide variety of equity research, sales and trading services to institutional, corporate and retail clients as well as providing an integrated service in equity derivatives, convertibles and portfolio trading.

Merchant banking — this business encompasses project and export finance, aviation and structured finance, syndicated finance, HSBC Equator and Amanah Finance. Project and export finance offers non-recourse financing to exporters, importers, and financial institutions, working closely with all major credit export agencies. Aviation and structured finance provides advice and financing for complex and tax efficient investment facilities, utilising international operations to facilitate cross-border transactions. Syndicated finance is integrated into the bank's debt financing and advisory platform and draws together structured finance, syndicated finance, debt capital and advisory services. HSBC Equator provides merchant, investment banking and commercial banking services throughout sub-Saharan Africa. Amanah Finance develops and structures products that are consistent with Islamic laws for its private client, institutional and corporate customers.

Private equity — the HSBC group offers institutional investors in Europe, Asia and the Americas the opportunity to invest in unlisted equities, including corporate restructurings, acquisition finance and development capital. Terms have been agreed to sell the fund management activities of HSBC Private Equity Limited to its management. The bank will retain a 19.9 per cent interest in the company which will be renamed Montagu Private Equity Limited. It is anticipated that the transaction will be completed by the end of the first quarter of 2003.

International Banking

International Banking provides financial services, primarily across Europe, including wealth management (personal and private banking, retail stockbroking and funds management) to local and expatriate customers, and wholesale banking (corporate, small commercial and investment banking, trade finance, payments and cash management and treasury services) to corporate and institutional clients. At the end of 2002, it had offices in 25 countries and territories.

Turkey — the bank acquired Demirbank TAS in October 2001 and, for the first time, the full year results of this business are reflected in the accounts. During 2002, the operations and business activities of Demirbank were successfully integrated and merged with those of HSBC Bank A.S. The combined operation now serves customers through a variety of channels: 163 branches, call centres, ATMs and internet banking.

On 19 September 2002, HSBC Bank A.S. completed the purchase of Turkey's largest independent consumer finance and card services company, Benkar, and its high-profile 'Advantage' brand. At the time of acquisition, Benkar had over 280 participating merchant firms and over one million Advantage card holders. The Advantage card can be used at over 5,000 points-of-sale in Turkey. The customer base has now been integrated into HSBC Bank A.S.

Offshore — HSBC Bank International Limited is the HSBC Group's dedicated provider of offshore financial and wealth management services for expatriate customers worldwide. The value of the HSBC Group offshore proposition to customers has been evidenced by a year-on-year growth in investment transactions achieved in difficult investment market conditions. To cater exclusively for the needs of expatriates and customers with international banking and investment requirements, HSBC Bank International Limited established a branch in the Hong Kong SAR and implant operations within the HSBC Group branches in Singapore and South Africa. Working in close co-operation with local HSBC Group entities, these offices service existing customers and also advise potential customers on offshore banking and investment products.

The business has recently received three highly commended awards from the *International Investment* magazine, in association with Standard and Poor's, in the categories of 'Best Offshore Banking Group', 'Best Technology Service' and 'Best Offshore Fund'.

Wealth management sales, including funds, investments, life and pension products and services continue to be a key strategic aim. The international funds distribution team has facilitated sales of over £650 million into a broad spectrum of offshore investment products, across 65 HSBC Group entities in 50 countries and territories.

Malta — several new products were launched including a world growth fund, an international bond fund, an equity-linked deposit account and a new home loan product 'Homestart', specifically targeted at first time buyers.

A number of initiatives have taken place to improve operational efficiencies, including the centralisation of back office credit administration and the processing of trade services products and activities.

Greece — HSBC Gold and Classic Visa credit cards were launched during the year, extending the product offering to the enlarged personal customer base following the acquisition of the Barclays branch network in 2001.

Russia — following a strategic review of the bank's operations in Moscow, additional capital has been injected and new staff recruited to support growth in corporate business.

Central Asia — Kazakhstan continued to grow its business with both multinational and local companies, resulting in an increased balance sheet and improved financial results.

CCF

Retail and commercial banking operations of CCF comprise the parent company with 226 branches and a network of 10 regional banks, with a total of 556 branches. Each regional bank operates in a specific geographical area with very strong local market representation under its own brand name. These include Banque Hervet (Paris and central France), Société Marseillaise de Crédit (Provence and south of France) and Union de Banques à Paris.

CCF offers retail products and services through a number of complementary distribution channels, such as online (www.ccf.fr), telephone and mobile phone banking. CCF's online brokerage service was launched in 1999, providing customers and non-customers alike with trading opportunities on the Paris Bourse. In addition, financial information including stock quotes, French and international

Business Description (continued)

newswires and research is also available. CCF's online credit company, Netvalor, offers credit for large household purchases directly to consumers through its dedicated consumer credit site (www.123credit.com).

The CCF networks also offer high-quality products and services to medium-sized French corporates and, in the regional subsidiaries, to entrepreneurs. CCF provides a number of online account management products and services, comprising trade account management, business intelligence, centralised corporate treasury management, electronic payments systems and the recovery of unpaid receivables, all branded under its 'Elys' product line. In addition, CCF delivers secure payment facilities that permit merchants to manage order and inventory functions and conduct bank transactions simultaneously.

CCF offers equity and corporate finance services, with teams integrated within the group. It advises on transactions involving notably French, British and international clients across a wide range of industries including retailing, chemicals, pharmaceuticals, banking, finance and insurance and entertainment. CCF has been one of the most active French banks advising on privatisations in France, where it has built a strong reputation. CCF is actively involved in significant debt and equity issues, including initial public offerings on the Paris Bourse. It also provides asset financing as well as structured financing for many well known corporates. Through a specialised subsidiary, Sinopia, CCF gives investment advice and third-party fund management in connection with commercial and residential real estate investment.

CCF supplies asset management services, primarily through three full-service fund management firms that serve institutional clients, as well as retail networks, with proprietary or non-proprietary products. HSBC Asset Management (Europe) SA is a major global mainstream discretionary manager; Sinopia specialises in active quantitative management together with guaranteed and structured products. HSBC Multimanager (Europe) is an independent service provider for fund selection and multi-management.

Elysées Fonds is a subsidiary that has a strong presence in the corporate savings plan market.

CCF offers a wide range of insurance products, including comprehensive health insurance, personal property casualty insurance and homeowners' insurance through its associated companies Erisa and Erisa IARD.

The private banking business has grown both organically and through the selective acquisition of a number of specialist institutions, including Banque du Louvre, Banque Eurofin, and Banque Dewaay (in Brussels) and through the transfer of HSBC Bank France S.A. in July 2002 from Private Banking.

Private Banking

The group's principal private banking activities are grouped under a Swiss holding company, HSBC Private Banking Holdings (Suisse) SA. As at 31 December 2002, subsidiary banks comprised HSBC Guyerzeller Bank AG and the international private banking operations of HSBC Republic located in Guernsey, the Hong Kong SAR, Jersey, London, Luxembourg, Monaco, Nassau, Singapore, and Switzerland.

Client services include advisory portfolio management, discretionary asset management, tax, trust and estate planning, mutual funds, and currency and securities transactions, as well as lending on a collateralised basis.

Private banking activities achieved a 10 per cent growth in funds under management in 2002, despite the fall in world stock markets.

Considerable progress was made during the year in regrouping the HSBC Group's private banking activities under HSBC Private Banking Holdings (Suisse) SA. This coherent ownership structure brings together the full range of both onshore and offshore private banking services to a growing customer base of predominantly European, Middle Eastern and Latin American high net worth individuals and their families.

The reorganisation of private banking operations in Asia under HSBC Republic Bank (Suisse) was completed in 2002 and HSBC Republic is now one of the region's three largest private banks. The operations infrastructure was rationalised to take advantage of scale efficiencies and clients were segmented according to both their needs and size of portfolio.

As part of a strategic objective to align onshore and offshore private banking operations, domestic and international private banking operations in the United Kingdom were successfully unified. The combined business of HSBC Republic Bank (UK) Limited was transferred to HSBC Private Banking Holdings (Suisse) SA, effective from 1 July 2002.

In June 2002, HSBC Guyerzeller Bank AG, which focuses on discretionary management and trustee services, completed the integration of Handelsfinanz-CCF Bank SA and Crédit Commercial de France (Suisse) SA. This initiative greatly strengthens Private Banking's presence in Geneva and provides important synergies and long-term cost savings.

During 2002, HSBC Private Banking Holdings (Suisse) also acquired HSBC Republic Holdings (C.I.) Limited, HSBC International Trustee Limited and HSBC Financial Services (Cayman) Limited, adding a further £39 billion in total client assets under management.

Private Banking has actively sought to increase credit services to clients and has succeeded in growing the lending book by 22 per cent. The trust business in Asia and the Channel Islands has been expanded and, working closely with HSBC Group Insurance, new tax efficient insurance products have been launched. Private Banking's range of investment funds continued to expand, especially in the alternative and hedge fund sector. The Hermitage Fund, the largest public equity fund dedicated to Russia, continues to be rated as one of the best performing equity funds in emerging markets.

Following successful trials in Asia during 2001, the roll-out of internet banking services to clients in the United Kingdom and Switzerland was completed in 2002. There are now over 5,400 registered clients. This facility will be extended to other Private Banking locations during 2003.

Working closely with HSBC Bank plc's retail banking operations has led to a significant increase in client referrals and to the introduction of business to other areas of the HSBC Group.

HSBC Trinkaus & Burkhardt

HSBC Trinkaus & Burkhardt KGaA (HSBC Trinkaus & Burkhardt) based in Düsseldorf, Germany, has branches in seven major German cities and has a subsidiary bank, HSBC Trinkaus & Burkhardt (International) SA, in Luxembourg.

A partnership limited by shares, quoted on German stock exchanges, HSBC Trinkaus & Burkhardt is directed by five personally liable managing partners. It preserves the 200-year heritage of a private bank, with the great flexibility and creativity that its size and structure fosters, while leveraging the advantages of the HSBC Group's worldwide reach and capabilities.

HSBC Trinkaus & Burkhardt offers a comprehensive range of services to wealthy private clients, large- and medium-size enterprises, institutional investors, public corporations and financial institutions. Its particular strengths lie in portfolio management, international business, interest rate and currency management, new issues on the debt and capital markets, corporate finance and mergers and acquisitions advisory. It has built a considerable reputation for innovative new issues, and for the delivery of well-designed products and services tailored to clients' distinctive requirements. Client business is strongly underpinned by trading activities in foreign exchange and interest rate products, and with leading positions through market-making in equities and equities derivatives trading.

HSBC Trinkaus & Burkhardt increased its stake in the funds management company Internationale Kapitalanlagegesellschaft mbH from 60 per cent to 100 per cent during 2002, recognising the strategic importance of developments in securities markets in Germany. Other subsidiaries include HSBC Trinkaus Capital Management GmbH, which provides investment advisory services, and HSBC Trinkaus & Burkhardt Immobilien GmbH, which primarily manages investments in closed-end property funds.

Funds under management at 31 December 2002 totalled £18 billion, more than double the size of the consolidated balance sheet of £7.2 billion.

In November 2002, HSBC Trinkaus & Burkhardt successfully implemented a new securities back office system, Geos, which delivers state-of-the-art processing and will enable the in-sourcing of back office processing in 2003.

Financial Review

Summary of Financial Performance

Consolidated Profit and Loss Account

	2002 £m	2001* £m
Net interest income	**4,039**	3,531
Other operating income	**3,653**	3,447
Operating income	**7,692**	6,978
Administrative expenses	**(4,060)**	(3,682)
Depreciation	**(455)**	(437)
Amortisation of goodwill	**(482)**	(460)
Operating profit before provisions	**2,695**	2,399
Provisions		
— provisions for bad and doubtful debts	**(377)**	(308)
— provisions for contingent liabilities and commitments	**(27)**	(34)
Amounts written off fixed asset investments	**(146)**	(29)
Operating profit	**2,145**	2,028
Share of operating (loss)/profit in joint ventures and associates	**(4)**	29
Gains/(losses) on disposal of		
— interests in joint ventures and associates	**32**	166
— investments	**122**	58
— tangible fixed assets	**(10)**	9
Profit on ordinary activities before tax	**2,285**	2,290
Tax on profit on ordinary activities	**(808)**	(722)
Profit on ordinary activities after tax	**1,477**	1,568
Minority interests		
— equity	**(30)**	(28)
— non-equity	**(68)**	(70)
Profit attributable to shareholders	**1,379**	1,470

** Figures for 2001 have been restated to reflect the adoption of UK Financial Reporting Standard 19, 'Deferred Tax', details of which are set out in Note 1(d) on the Accounts on page 64.*

A number of acquisitions and business transfers affect the comparison between 2001 and 2002. These include the full year effect of the transfer of Asian business into Private Banking from April 2001, the acquisition of Banque Hervet by CCF in July 2001, the acquisition of Demirbank TAS ('Demirbank') in October 2001 and of HSBC Guyerzeller Bank AG in December 2001. During 2002, the bank integrated further private banking activities, acquired Benkar Tuketici Finansmani ve Kart Hizmetleri AS ('Benkar') in September 2002 and transferred from other parts of the HSBC Group, HSBC Trinkaus & Burkhardt KGaA and HSBC Select (UK) Limited in July 2002 and HSBC Investment Banking activities and Merrill Lynch HSBC Limited in November 2002. The effect of acquisitions and transfers in 2002 increased operating profit by £36 million.

Operating profit before provisions, at £2,695 million, grew by £296 million, or 12 per cent, over 2001. Profit before tax of £2,285 million increased by £134 million, or 6 per cent, if the £139 million profit from the sale of the bank's shareholding in British Interactive Broadcasting in 2001 is excluded. Despite competitive pressures on spreads and a general downturn in market activity, particularly amongst corporate and financial institutions, operating income was up by 10 per cent. Operating expenses increased, mainly due to acquisitions and transfers, and bad debt charges grew, due to higher charges in Corporate and Institutional Banking. There was a significant write-down of fixed asset investments within CCF.

Net interest income

	2002	2001
Net interest income (£m)	**4,039**	3,531
Average interest-earning assets (£m)	**178,302**	156,915
Gross interest yield[1] (%)	**4.65**	6.04
Net interest spread[2] (%)	**1.96**	1.73
Net interest margin[3] (%)	**2.27**	2.25
HSBC Bank plc UK base lending rate (%)	**4.0**	5.1
London interbank offered rate ('LIBOR')		
Three months pounds sterling (%)	**3.9**	5.0
Six months eurodollar (%)	**2.0**	3.7
Six months euro (%)	**3.4**	4.2
US prime rate (%)	**4.7**	6.9

1 Interest yield is the average interest rate earned on average interest-earning assets.
2 Interest spread is the difference between the average interest rate earned on average interest-earning assets and the average interest rate paid on average interest-bearing funds.
3 Interest margin is net interest income as a percentage of average interest-earning assets.

Net interest income improved by £508 million, or 14 per cent, to £4,039 million, with underlying growth of 10 per cent, if the effect of business transfers and acquisitions is excluded. Average interest-earning assets increased by £21.4 billion, or 14 per cent, with higher balances in Private Banking, following the integration of a number of private banking activities in 2001 and 2002. Mortgage lending increased as more customers took advantage of the low interest rate environment and competitiveness of the bank's product, and there was growth in other personal and commercial lending. Personal and commercial current account balances also increased, by 11 per cent and 14 per cent respectively. The income benefit from these higher balances was reduced by the effect of lower interest rates. Assets increased in UK Treasury and Capital Markets, where surplus funds were invested in investment grade corporate and institutional bonds, and from stock lending business, transferred from another part of the HSBC Group.

Interest spread increased by 23 basis points to 1.96 per cent, primarily due to UK Treasury and Capital Markets which benefited from lower rates on money market liabilities as short-term sterling and US interest rates fell. Spreads increased on personal customer lending and savings products. The increase in interest spread was offset by the reduced value of free funds following the reduction in interest rates. Margin was slightly improved at 2.27 per cent.

Other operating income

	2002 £m	2001 £m
Dividend income	**114**	33
Fees and commissions receivable	**3,161**	2,806
Fees and commissions payable	**(560)**	(460)
Foreign exchange	**357**	321
Interest rate derivatives	**5**	41
Debt securities	**37**	39
Equities and other trading	**(11)**	41
Dealing profits	**388**	442
Operating lease income	**327**	323
Increase in the value of long-term assurance business attributable to shareholders	**84**	140
Other	**139**	163
Other operating income	**3,653**	3,447

Other operating income grew by 6 per cent to £3,653 million in difficult market conditions, reflecting the effect of acquisitions and business transfers into the bank and growth in fees and commissions income and increased dividend income. Growth in dividend income from equities swaps trading was achieved in UK Treasury and Capital Markets at the expense of lower equities and other trading income. This was

Financial Review (continued)

partly offset by a £36 million reduction in dealing profits from interest rate derivatives, largely due to CCF losses incurred on interest arbitrage activities on securities and difficult market conditions. Net fees and commissions income rose by £255 million or 11 per cent to £2,601 million. Private Banking generated £121 million of this additional income in 2002, with the integration of private banking activities transferred from other parts of the HSBC Group contributing £112 million of the growth. The addition of HSBC Trinkaus & Burkhardt KGaA and Investment Banking contributed £63 million to fees and commissions. Sales of general insurance, life, critical illness and income protection products also increased, and there was higher fee income from commercial overdrafts. Income from Turkey grew, reflecting 12 months income in Demirbank and the acquisition of the Benkar credit card business. In addition, there was higher income from Treasury activities which benefited from growth in bond origination activities, where the continued alignment with HSBC Group's corporate clients resulted in increased revenues. The growth in operating income was partly offset by a reduction in life, pensions and investment income, as a result of the fall in the investment markets and adjustments to the value of long-term assurance business.

	2002			2001		
	Dealing profits £m	**Dividend and net interest income £m**	**Total £m**	Dealing profits £m	Dividend and net interest income £m	Total £m
Foreign exchange	**357**	**17**	**374**	321	(2)	319
Interest rate derivatives	**5**	**1**	**6**	41	11	52
Debt securities	**37**	**74**	**111**	39	24	63
Equities and other trading	**(11)**	**31**	**20**	41	5	46
	388	**123**	**511**	442	38	480

The table above shows the total of dealing profits and dividend and net interest income attributable to dealing activities, but excludes the cost of associated staff and other administrative expenses. The net interest income on securities trading arises on mark-to-market debt securities and treasury bills.

Securities held for dealing purposes include British Government Securities, other government securities and securities issued by banks and corporates.

Operating expenses

	2002 £m	2001 £m
Staff costs	**2,507**	2,334
Premises and equipment (excluding depreciation)	**545**	466
Other administrative expenses (excluding amortisation)	**1,008**	882
Administrative expenses	**4,060**	3,682
Depreciation	**455**	437
Amortisation of goodwill	**482**	460
Operating expenses	**4,997**	4,579
Cost:income ratio (excluding amortisation of goodwill)	**58.7%**	59.0%
Full-time equivalent staff numbers at 31 December	**70,633**	65,583

In 2002, operating expenses increased by £418 million, or 9 per cent, to £4,997 million. Excluding the amortisation of goodwill and the full year impact of acquisitions and transfers into the group, including private banking businesses, Banque Hervet, Investment Banking, HSBC Trinkaus & Burkhardt KGaA, expansion in Turkey, HSBC Select (UK) Limited and Merrill Lynch HSBC Limited, underlying costs increased by £63 million or 2 per cent. Demand for remote services continues to grow and the bank is responding with further investment in internet banking and ATMs, expansion of its global processing capability, and further development of the bank's customer relationship management system. Excluding the impact of the acquired and transferred entities, staff costs were broadly in line with 2001. Outsourcing of the bank's cash and cheque processing services led to some savings in staff costs, though fees for outsourced activities are included within administrative expenses. The full cost savings from outsourcing will not be seen until future years. The growth in full-time equivalent staff reflected the transfer of the Investment Bank and private banking activities, HSBC Trinkaus & Burkhardt KGaA, HSBC Select (UK) Limited and Merrill Lynch HSBC Limited and the acquisition of Benkar. Non-staff costs, excluding the amortisation of goodwill and costs of the entities acquired and transferred to the group, were 5 per cent higher, reflecting increased business volumes and IT processing capacity. The phased move of the bank's headquarters to Canary Wharf began in August 2002 with related one-off costs, including provisions for vacant space of £26 million in 2002 compared with an £11 million recovery in 2001, and diminution in value of certain London properties, £22 million compared with £6 million in 2001, reflecting the weakness of the London property market. Spending on promoting the HSBC brand was increased and significant progress was made towards building the HSBC Group's differentiated brand positioning 'The world's local bank'. However, overall marketing costs in 2002 were lower compared with 2001. The group's cost:income ratio, excluding the amortisation of goodwill, improved to 58.7 per cent.

Provisions for bad and doubtful debts

	2002 **£m**	2001 £m
Analysis of total charge		
— new provisions	**633**	542
— releases and recoveries	**(221)**	(220)
— charge for specific provisions	**412**	322
— release of general provisions	**(35)**	(14)
	377	308

	2002 **%**	2001 %
Total customer provisions as a percentage of gross loans and advances to customers	**2.1**	2.3
General provisions as a percentage of net loans and advances to customers	**0.5**	0.6
As a percentage of average gross loans and advances to banks and customers for the year:		
charge for specific provisions	**0.3**	0.3
total provisions charged	**0.3**	0.3
amounts written off net of recoveries	**0.2**	0.2

The charge for bad and doubtful debts was £69 million or 22 per cent higher than in 2001. New specific provisions increased by £91 million mainly as a result of a small number of large corporate provisions in the telecommunications sector. There were also some significant individual new provisions for commercial loans to the private health, leisure and manufacturing sectors. By contrast, the bad debt performance of Personal Banking improved in 2002. There was also a lower level of bad debts within International Banking, mainly reflecting reduced provisions within Offshore. Continued tight risk control in CCF saw a reduced corporate bad debt charge. There was a £35 million net release of general provisions in 2002, mainly within the UK business. This release reflected a reduction in estimated latent loan losses, which had occurred at the balance sheet date but which had not yet been reflected through the establishment of specific provisions. The estimate of these latent losses reflects the group's historical experience of the rate at which such losses occur and are identified, the structure of the credit portfolio and the economic and credit conditions prevailing at the balance sheet date. This followed a £14 million net release of general provisions in 2001, following a reassessment of the level of provisions required by Private Banking.

Amounts written off fixed asset investments

In 2002, the amounts written off fixed asset investments increased by £117 million to £146 million, mainly in CCF following the write-down of a strategic equity investment in a European life insurance company.

Financial Review (continued)

Share of operating (loss)/profit in joint ventures and associates

Profit from joint ventures and associates declined by £33 million, mainly in CCF, due to the effect of lower stock markets on its French insurance and UK asset management activities.

Gains/(losses) on disposal

Gains on disposal of investments, at £122 million, were £64 million higher than in 2001 and included gains from the sale of Lixxbail and private equity investments in CCF, from the sale of an equity investment in UK Personal Banking and from the liquidation of a Russian Recovery Fund in Private Banking.

Gains on disposal of interests in joint ventures and associates were £134 million lower than in 2001, mainly due to the sale of the bank's shareholding in British Interactive Broadcasting in 2001.

Taxation

In 2002, the effective tax rate increased to 35.4 per cent from 31.5 per cent in 2001 (as restated under FRS 19, 'Deferred Tax'), primarily due to smaller capital profits offset against available losses, higher overseas taxation from overseas operations and additional property write-down charges not allowable for tax purposes.

Results of Business Segments

In accordance with the HSBC Group's 'Managing for Value' strategy, the group has segmented its business into the following categories: UK Personal Banking; UK Commercial Banking; UK Corporate and Institutional Banking; UK Treasury and Capital Markets; Investment Banking; International Banking; CCF (formerly Crédit Commercial de France); Private Banking (formerly HSBC Republic); and HSBC Trinkaus & Burkhardt. Segments have been reported on a cash basis, which excludes the amortisation of goodwill.

Central items have been allocated across all segments. Interest on central capital has been allocated based on average risk-weighted assets and other regulatory capital requirements, where appropriate. Other central items have been allocated according to the respective business activities of the appropriate segment. This has required some judgement to be made in the allocation process. In particular, substantial costs involved in the delivery of services are not specific to any one particular business segment.

Profit on ordinary activities before tax for 2002 and 2001 is summarised in the table below:

	2002 £m	2001 £m
Operating profit — cash basis		
UK Personal Banking	**539**	468
UK Commercial Banking	**630**	558
UK Corporate and Institutional Banking	**312**	494
UK Treasury and Capital Markets	**451**	331
Investment Banking	**(2)**	—
Corporate, Investment Banking and Markets	**761**	825
International Banking	**213**	196
CCF	**258**	270
Private Banking	**209**	171
HSBC Trinkaus & Burkhardt	**17**	—
Operating profit — cash basis	**2,627**	2,488
Amortisation of goodwill*	**(482)**	(460)
Share of operating (loss)/profit in joint ventures and associates	**(4)**	29
Gains on disposal of interests in joint ventures and associates	**32**	166
Gains on disposal of investments and tangible fixed assets	**112**	67
Profit on ordinary activities before tax	**2,285**	2,290

** The amortisation of goodwill includes £303 million (2001: £304 million) in respect of CCF and £169 million (2001: £147 million) in respect of Private Banking.*

UK Personal Banking

	2002 £m	2001 £m
Cash basis		
Net interest income	**1,301**	1,128
Other operating income	**830**	891
Operating income	**2,131**	2,019
Administrative expenses	**(1,345)**	(1,302)
Depreciation	**(98)**	(98)
Operating profit before provisions	**688**	619
Provisions for bad and doubtful debts	**(133)**	(148)
Provisions for contingent liabilities and commitments	**(15)**	(2)
Amounts written off fixed asset investments	**(1)**	(1)
Operating profit	**539**	468
Gains on disposal of interests in associates	**—**	139
Gains/(losses) on disposal of investments and tangible fixed assets	**16**	(1)
Profit on ordinary activities before tax	**555**	606

In 2002, UK Personal Banking's operating profit before provisions at £688 million grew by £69 million, or 11 per cent, over 2001. Profit before tax of £555 million was £51 million lower than in 2001, or 19 per cent higher, after excluding the £139 million profit from the sale of the bank's shareholding in British Interactive Broadcasting in 2001.

In July 2002, HSBC Select (UK) Limited, a specialist insurance company, was transferred from another part of the HSBC Group, while in November Merrill Lynch HSBC Limited was integrated into the UK Personal Banking business.

Net interest income of £1,301 million increased by 15 per cent, reflecting strong growth in sales of both lending and savings products. The reduction in the spread on current accounts arising from lower interest rates was wholly offset by an 11 per cent increase in balances. Growth of 19 per cent was achieved in savings balances, which also benefited from a widening of spreads. Mortgage balances grew by £3.6 billion, up 24 per cent. Gross new mortgage lending increased by 57 per cent as a result of the buoyant housing market and the bank's competitive products. The bank's share of the overall increase in UK mortgage lending rose from 4.4 per cent in 2001 to 5.8 per cent in 2002.

Other operating income fell by 7 per cent to £830 million. Sales of general insurance, life, critical illness and income protection grew strongly and the bank's combined market share for its principal investment products, Open Ended Investment Companies and ISAs, was maintained at over 5 per cent in 2002, despite difficult investment market conditions. However, overall wealth management income reduced, principally as a result of the fall in the investment markets and adjustments to the value of long-term assurance business. This was partly offset by the impact of the transfer of HSBC Select (UK) Limited.

Operating expenses increased by 3 per cent to £1,443 million partly as a result of the integration of Merrill Lynch HSBC Limited and HSBC Select (UK) Limited. Excluding these transfers, underlying costs went up by £31 million, or 2 per cent, partly reflecting increased investment in customer contact activities and systems development.

The charge for bad and doubtful debts fell by £15 million, or 10 per cent, and included a £10 million general provision release. There was a lower specific charge on personal lending though the bank maintained its credit standards.

Gains on disposal of interests in associates in 2001 reflected the sale of the bank's shareholding in British Interactive Broadcasting.

Financial Review (continued)

UK Commercial Banking

	2002 £m	2001 £m
Cash basis		
Net interest income	**745**	699
Other operating income	**735**	680
Operating income	**1,480**	1,379
Administrative expenses	**(611)**	(596)
Depreciation	**(142)**	(143)
Operating profit before provisions	**727**	640
Provisions for bad and doubtful debts	**(97)**	(78)
Amounts written off fixed asset investments	**—**	(4)
Operating profit	**630**	558
Share of operating (loss)/profit in joint ventures and associates	**(2)**	1
(Losses)/gains on disposal of investments and tangible fixed assets	**(1)**	4
Profit on ordinary activities before tax	**627**	563

In 2002, UK Commercial Banking's operating profit before provisions at £727 million grew by £87 million, or 14 per cent, over 2001. Despite challenging market conditions, profit before tax rose by 11 per cent to £627 million, largely driven by growth in operating income.

Net interest income rose by 7 per cent to £745 million, reflecting growth in current accounts, deposits and term lending. Current account balances increased by 14 per cent to £6.1 billion but the impact was partly offset by narrower spreads as a result of lower interest rates. Deposit balances grew by 9 per cent and spreads also improved. Sterling term lending balances grew by 9 per cent during the year, with average balances per customer also rising, and spreads widened. The bank increased its share of business start-ups, with more than 87,000 new business accounts opened in 2002. The number of customers moving from competitors to the bank also increased and contributed to a 7 per cent increase in the number of customers.

Other operating income at £735 million was 8 per cent higher than in 2001. Growth in the number of customers helped to contribute to a £22 million increase in fee income from business overdrafts. Cards income grew by 6 per cent. Invoice finance income grew by £8 million with a 13 per cent rise in client numbers opting for credit protection.

Operating expenses were £753 million, £14 million higher than in 2001. The bank continued to invest in a variety of alternative sales channels and more than 132,000 customers are now registered to use the bank's business telephone banking centres located in the UK and India. Business internet banking was introduced in January 2002 and extends electronic banking to the bank's smaller business customers. Over 35,000 customers have been attracted to this service since its introduction.

The charge for bad and doubtful debts rose by 24 per cent to £97 million. New provisions were made for loans to customers in the private health, leisure and manufacturing sectors against a general deterioration in economic conditions in 2002.

UK Corporate and Institutional Banking

	2002 £m	2001 £m
Cash basis		
Net interest income	**266**	277
Other operating income	**461**	496
Operating income	**727**	773
Administrative expenses	**(230)**	(205)
Depreciation	**(90)**	(79)
Operating profit before provisions	**407**	489
Provisions for bad and doubtful debts	**(95)**	4
Provisions for contingent liabilities and commitments	**—**	1
Operating profit	**312**	494
Profit on ordinary activities before tax	**312**	494

In 2002, UK Corporate and Institutional Banking's operating profit before provisions fell by 17 per cent to £407 million. Profit before tax of £312 million was £182 million, or 37 per cent, lower than in 2001, reflecting lower fee income and a charge for bad debt provisions, compared with a recovery in the previous year.

Net interest income fell by £11 million, or 4 per cent, due principally to a reduced value of free funds and a narrowing spread on deposit accounts. These effects were partly offset by an increase in current account balances and improved term lending spreads. Bringing together corporate, treasury and investment banking has enabled customers to access different debt markets more readily and has tended to lead to flat lending balances. The success in bond origination has increased income reported within UK Treasury and Capital Markets.

Other operating income was £35 million, or 7 per cent, lower than in 2001. This reflects the impact of subdued stock market activity on the custody services business and lower fee income from reduced corporate activity.

Operating expenses at £320 million were £36 million or 13 per cent higher than in 2001. Increased operating lease assets, largely railway rolling stock, have contributed to a higher depreciation charge. Additional costs have been incurred by a programme of restructuring within the bank and increased resourcing to support pan-European business, ensuring that the bank's client-focused service meets all the needs of its corporate and institutional clients.

The charge for bad and doubtful debts of £95 million reflected a small number of large provisions in the telecommunications sector and compares with a small net recovery in 2001.

UK Treasury and Capital Markets

	2002 £m	2001 £m
Cash basis		
Net interest income	**391**	297
Other operating income	**267**	220
Operating income	**658**	517
Administrative expenses	**(190)**	(175)
Depreciation	**(17)**	(14)
Operating profit before provisions	**451**	328
Provisions for bad and doubtful debts	**—**	3
Operating profit	**451**	331
Gains on disposal of investments and tangible fixed assets	**16**	7
Profit on ordinary activities before tax	**467**	338

In 2002, UK Treasury and Capital Markets' operating profit before provisions grew strongly as uncertain world markets and low interest rates provided opportunities in money markets, fixed income and emerging markets. Profit before tax increased by £129 million, or 38 per cent, to £467 million.

Financial Review (continued)

Net interest income increased by 32 per cent primarily due to the continuing benefit of reduced funding costs following the decline in short-term interest rates in 2001. In addition, significant net interest income was generated as the bank increased the deployment of its surplus liquidity into investment grade corporate and institutional bonds.

Other operating income rose by £47 million, or 21 per cent. Higher foreign exchange income reflected strong growth from currency options where volumes more than doubled over 2001. There was also increased activity in the trading of emerging markets currencies. Fixed income benefited from growth in bond origination activities, where the alignment with HSBC Group's corporate clients resulted in higher revenues. Gilt trading performance also improved.

Operating expenses were £18 million, or 10 per cent higher than in 2001, mainly due to higher staff costs, as staff bonuses rose in line with the improvement in performance.

Investment Banking

The investment banking activities of HSBC Investment Bank plc were transferred into the bank on 30 November 2002 as part of the HSBC Group's drive to align its corporate and investment banking activities. The impact of this transfer on profit before tax was minimal and, as a result, no analysis of profit before tax has been disclosed.

International Banking

	2002 £m	2001 £m
Cash basis		
Net interest income	**375**	310
Other operating income	**201**	192
Operating income	**576**	502
Administrative expenses	**(292)**	(220)
Depreciation	**(30)**	(23)
Operating profit before provisions	**254**	259
Provisions for bad and doubtful debts	**(37)**	(59)
Provisions for contingent liabilities and commitments	**(1)**	2
Amounts written off fixed asset investments	**(3)**	(6)
Operating profit	**213**	196
Losses on disposal of investments and tangible fixed assets	**(5)**	(3)
Profit on ordinary activities before tax	**208**	193

In 2002, International Banking reported an operating profit before provisions of £254 million, broadly in line with last year. Profit before tax of £208 million was 8 per cent higher than in 2001. The improvement in profit reflected reduced bad debt provisions. Turkey contributed £62 million of operating profit following the integration of Demirbank and the acquisition of Benkar in September 2002. Profits in Malta increased, benefiting from lower funding costs and reductions in headcount.

Net interest income at £375 million increased by 21 per cent over 2001 and reflected the integration of Demirbank's personal banking portfolio and the purchase of Benkar. Offshore increased by 10 per cent following growth in current and savings accounts and in mortgages.

Other operating income increased by 5 per cent, benefiting from the inclusion of the credit card portfolios of Demirbank and Benkar. In Offshore, income from the sales of investment products declined in the face of uncertain equity markets and lower investor confidence.

Operating expenses increased by 33 per cent to £322 million, largely as a result of the acquisitions in Turkey. Continued investment made in the international network was balanced by operating efficiencies in Greece and Malta.

The charge for bad and doubtful debts was £22 million lower than in 2001 as a result of reduced provisions in the Offshore, Malta and Turkey businesses.

CCF

	2002 £m	2001 £m
Cash basis		
Net interest income	**681**	618
Other operating income	**707**	749
Operating income	**1,388**	1,367
Administrative expenses	**(928)**	(931)
Depreciation	**(63)**	(69)
Operating profit before provisions	**397**	367
Provisions for bad and doubtful debts	**(12)**	(54)
Provisions for contingent liabilities and commitments	**(1)**	(25)
Amounts written off fixed asset investments	**(126)**	(18)
Operating profit	**258**	270
Share of operating profit in joint ventures and associates	**12**	28
Gains on disposal of interests in joint ventures and associates	**32**	27
Gains on disposal of investments and tangible fixed assets	**63**	46
Profit on ordinary activities before tax	**365**	371
Cost:income ratio	**71.4%**	73.2%

The integration and alignment of CCF within the HSBC Group continued in 2002. Management responsibilities for the HSBC Group's businesses in France, Spain, Italy, Belgium and the Netherlands were assumed by CCF, although their results continued to be reported within International Banking. In 2001, CCF's private banking operations in Switzerland, Monaco and Luxembourg were merged with HSBC Republic's existing operations to maximise synergies and in exchange CCF received shares in HSBC Republic. In March 2002, CCF sold HSBC Specialist Investments Limited to HSBC Asset Management and in June 2002 Lixxbail, CCF's joint venture leasing company, was sold to the other joint venture partner. In July 2002, CCF acquired HSBC Bank France S.A. from Private Banking and acquired 11 French regional branches from Banque Worms. Changes in CCF's corporate structure for the two years therefore complicate direct comparisons of the results.

Operating profit before provisions increased by £30 million or 8 per cent. Profit before tax reduced by £6 million, mainly due to the write-down of an investment in a European life insurance company, partly offset by an increased gain on disposal of investments.

Net interest income grew by £63 million, or 10 per cent, compared with 2001. There was growth in lending volumes to personal customers and strong growth in sight deposits due to the introduction of the euro and the uncertain economic and market environment. Banque Hervet, acquired in March 2001, contributed £23 million of additional net interest income. Treasury activities benefited from the lower interest rate environment and interest arbitrage activities on securities also boosted net interest income at the expense of dealing income.

Other operating income decreased by £42 million, or 6 per cent, largely due to a reduction in dealing profits, linked to the above movement in treasury activities and also to mark-to-market losses. The growing synergies between Paris, London and other European offices helped to win new mandates and to rank the HSBC Group first on the Eurocorporate bond league table for UK and French issuers and second for Spanish corporate bond issuance. CCF Network banking fees increased while stock market commissions were lower due to the depressed financial environment. Fees and commissions in CCF's regional banking subsidiaries increased moderately with growth in banking transaction fees, including sales of investment protection products, compensating for lower stock market commissions. Corporate and institutional banking fees increased strongly compared with the previous year, reflecting the growing synergies between CCF and the HSBC Group. Corporate finance fees were boosted by CCF's role as lead manager for the institutional placement of shares in Autoroutes du Sud de la France, the largest issue in the European market in 2002. Fees in stockbroking and market making dropped significantly compared with 2001, due to lower market activity. Asset management and private banking activities were also impacted by lower stock market indices.

Operating expenses decreased slightly despite the full year impact of Banque Hervet, due to the effect of business transfers. Underlying staff costs

Financial Review (continued)

were broadly unchanged compared with 2001, with a small decrease in headcount.

Bad and doubtful debt charges reduced by £42 million due to a lower corporate charge. Bad debt charges remain at a very low level due to continued tight risk control.

Provisions for contingent liabilities and charges fell significantly compared with the previous year which was impacted by a one-off item.

Amounts written off fixed asset investments largely reflected a write-down of a strategic equity investment in a European life insurance company.

CCF's share of operating profit in joint ventures and associates declined in 2002, largely due to the impact of lower stock markets on its French insurance and UK asset management associates.

Gains on disposal of investments, tangible fixed assets and interests in joint ventures and associates increased, following the sale of shareholdings in Lixxbail and Cedel and of various equity investments including the flotation of Intertek.

Private Banking

	2002 £m	2001 £m
Cash basis		
Net interest income	**246**	202
Other operating income	**357**	219
Operating income	**603**	421
Administrative expenses	**(359)**	(253)
Depreciation	**(11)**	(11)
Operating profit before provisions	**233**	157
Provisions for bad and doubtful debts	**—**	24
Provisions for contingent liabilities and commitments	**(12)**	(10)
Amounts written off fixed asset investments	**(12)**	—
Operating profit	**209**	171
Share of operating loss in joint ventures and associates	**(8)**	—
Gains on disposal of investments and tangible fixed assets	**24**	14
Profit on ordinary activities before tax	**225**	185
Cost:income ratio	**61.4%**	62.7%

HSBC Republic acquired the private banking entities of HSBC Holdings in the Hong Kong SAR and Singapore on 1 April 2001. Private Banking included the results of the following entities: from 31 December 2001, HSBC Guyerzeller Bank AG; from 1 January 2002, HSBC Private Banking (Bahamas) Limited; from 1 April 2002, HSBC Republic (Cayman) Limited, HSBC Republic Holdings (C.I.) Limited and HSBC International Trustee Limited; and from 1 July 2002, HSBC Republic Bank (UK) Limited. HSBC Bank France S.A.'s results were included in Private Banking's results up to 30 June 2002.

In 2002, Private Banking reported an operating profit before provisions of £233 million, 48 per cent higher than in 2001.

Net interest income grew by £44 million to £246 million. Excluding the effect of transferred entities, net interest income decreased by £14 million, due to the effect of lower interest rates on the investment portfolio, and on the value of free funds. Spread was also reduced by the sale of emerging market securities in late 2001 and early 2002.

Other operating income increased by £138 million, or by an underlying £9 million excluding the effect of the transferred entities. This increase was driven primarily through additional customer assets under management and their corresponding transaction and safekeeping fees, greater performance fees on the Private Banking funds, increased discretionary management fees and greater foreign exchange income from both client initiated trades and proprietary results. The Asian businesses performed strongly in 2002, with significant growth in income, while costs were reduced.

Operating expenses were 40 per cent higher than in 2001, but slightly lower excluding the effect of the transferred entities.

Net bad debt and contingent liabilities provisions and amounts written off investments were £24 million in 2002, compared with a credit of £14 million in the prior year. The current year included a specific write down of a debt security and provisions for contingent liabilities, while 2001 included a larger reduction in general provisions, following a reassessment of provisions required.

Gains on disposals of investments and fixed assets were £24 million in 2002, compared with £14 million in 2001, mainly reflecting a gain on liquidation of the Russian Recovery Fund established in 2000 to manage proprietary and client investments.

Total client assets under management grew by £50 billion to £105 billion, with £39 billion of the growth due to businesses transferred. Total trust assets grew from £2 billion to £49 billion within that total.

HSBC Trinkaus & Burkhardt

	2002 £m
Cash basis	
Net interest income	26
Other operating income	64
Operating income	90
Administrative expenses	(69)
Depreciation	(3)
Operating profit before provisions	18
Provisions for bad and doubtful debts	(3)
Provisions for contingent liabilities and commitments	2
Operating profit	17
Losses on disposal of investments and tangible fixed assets	(1)
Profit on ordinary activities before tax	16
Cost:income ratio	80.0%

HSBC Trinkaus & Burkhardt KGaA was transferred into the group from another part of the HSBC Group in July 2002.

The difficult economic environment in Germany had a negative impact on HSBC Trinkaus & Burkhardt's results in 2002, as subdued activity in the securities markets depressed both trading and client related business.

Fees and commissions benefited from strong corporate finance income, which offset a significant reduction in equity commissions as a result of lower transaction volumes. Trading income also suffered in the weak equity markets.

Strict cost controls led to a fall in operating expenses despite one-off costs relating to the successful implementation of a new securities system. Staff numbers fell slightly reflecting the reduction in market activity and lower transaction numbers.

Profits from corporate banking customers grew strongly in 2002 as a result of lower specific bad debt charges in an environment where corporate insolvencies reached a record high. Closer co-operation with other parts of the HSBC Group increased the flow of business from large corporate customers and helped deepen customer relationships. In addition, marketing activities with German Mittelstand companies proved to be increasingly successful.

Profits from private banking customers decreased following the steady fall in share prices during 2002. A significant inflow of new funds was unable to compensate for reductions in advisory fees and securities transaction commissions. Uncertainty on amendments to German tax laws, following the general elections in autumn 2002, also slowed the placement of closed-end property funds.

Despite reduced activities in the equity market, profit from the institutional clients business was largely unchanged. Increased interest in fixed interest and alternative investment products compensated for reduced equity related commissions. Co-operation with other HSBC Group members significantly improved the bank's market position in Fixed Income Origination and Sales.

Trading activities generally suffered from the weakness in equity markets and profits in the Equities Derivatives Group fell sharply as volatilities increased.

Financial Review (continued)

Capital Management

Capital measurement and allocation

The Financial Services Authority (FSA) is the supervisor of the bank and the group and, in this capacity, receives information on capital adequacy and sets minimum capital requirements. Individual banking subsidiaries are directly regulated by the appropriate local banking supervisors, which set and monitor capital adequacy requirements for them.

Under the European Union's Banking Consolidation and Amending Directive (Directive 98/31/EC) to the Capital Adequacy Directive ('CAD2'), the FSA requires each bank and banking group to maintain an individually prescribed ratio of total capital to risk-weighted assets.

The group's capital resources policy is to maintain its capital base through the diversification of its sources of capital and the efficient allocation of capital. It seeks to maintain at all times a prudent relationship between its total capital, as measured according to the criteria used by the FSA for supervisory purposes, and the varied risks of its business.

Capital adequacy is measured by the ratio of capital to risk-weighted assets, taking into account balance sheet assets and off-balance-sheet transactions, calculated for both the bank and the group on a consolidated basis.

The group's capital is divided into two tiers. Tier 1 comprises shareholders' funds, excluding revaluation reserves, and minority interests in tier 1 capital, and tier 2 comprises general loan loss provisions, property revaluation reserves, qualifying subordinated loan capital and minority and other interests in tier 2 capital.

Capital analysis

The table on page 29 is an analysis of the group's regulatory capital position and risk-weighted assets at 31 December 2002 and 2001.

The figures were computed in accordance with the EU Banking Consolidation Directive. The comparative figures for 2001 have not been restated to reflect the adoption of FRS19, details of which are set out in Note 1(d) in the Notes on the Accounts on page 64.

Tier 1 capital increased by £1,027 million in 2002. This was largely due to exchange rate movements of £359 million, the issue of shares amounting to £292 million and profit retentions of £235 million.

The decrease of £336 million in tier 2 capital in 2002 mainly reflects maturities, redemptions and regulatory amortisation, net of capital issues.

Total risk-weighted assets increased by £10.1 billion due to growth in customer lending and the transfer of business from HSBC Investment Bank plc.

Regulatory capital position

Composition of capital	2002 £m	2001 £m
Tier 1:		
Shareholders' funds	**16,455**	15,630
Minority interests	**334**	301
Innovative tier 1 securities	**586**	550
Less: property revaluation reserves	**(121)**	(166)
goodwill capitalised and intangible assets	**(8,490)**	(8,578)
Total qualifying tier 1 capital	**8,764**	7,737
Tier 2:		
Property revaluation reserves	**121**	168
General provisions	**480**	547
Undated subordinated loan capital	**1,354**	1,369
Qualifying dated subordinated loan capital	**2,389**	2,689*
Minority and other interests in tier 2 capital	**704**	611
Total qualifying tier 2 capital	**5,048**	5,384
Unconsolidated investments	**(782)**	(688)
Investments in other banks and other financial institutions	**(226)**	(202)
Other deductions	**(36)**	(22)
Total capital	**12,768**	12,209
Total risk-weighted assets	**123,864**	113,749
	%	%
Total capital: risk-weighted assets	**10.3**	10.7
Tier 1 capital: risk-weighted assets	**7.1**	6.8

** Restated to show separately the subordinated loan obligations of the Paris office.*

Market Risk Management

Market risk is the risk that interest rates, foreign exchange rates or equity and commodity prices will move and result in profits or losses to the group. Market risk arises on financial instruments which are valued at current market prices (mark-to-market basis) and those valued at cost plus any accrued interest (accruals basis).

The group makes markets in interest rate, exchange rate and equity derivative instruments, as well as in debt, equities and other securities. Trading risks arise either from customer-related business or from position taking.

The group manages market risk through risk limits approved by the HSBC Bank Executive Committee. Traded Markets Development and Risks, an independent unit within Investment Banking and Markets, develops risk management policies and measurement techniques and reviews limit utilisation on a daily basis.

Risk limits are determined for each location and, within location, for each portfolio. Limits are set by product and risk type, with market liquidity being a principal factor in determining the level of limits set. Only those offices with sufficient derivative product expertise and appropriate control systems are authorised to trade derivative products. Limits are set using a combination of risk measurement techniques, including position limits, sensitivity limits, as well as value at risk ('VAR') limits at a portfolio level. Similarly, option risks are controlled through full revaluation limits in conjunction with limits on the underlying variables that determine each option's value.

Trading VAR

VAR is a technique which estimates the potential losses that could occur on risk positions taken due to movements in market rates and prices over a specified time horizon and to a given level of confidence. The group's VAR, predominantly calculated on a variance/co-variance basis, uses historical movements in market rates and prices, a 99 per cent confidence level, a 10-day holding period, and generally takes account of correlations between different markets and rates, and is calculated daily. The movement in market prices is calculated by reference to market data from the last two years.

Aggregation of VAR from different risk types is based upon the assumption of independence between risk types.

The group VAR should be viewed in the context of the limitations of the methodology used. These include:

- The model assumes that changes in risk factors follow a normal distribution. This may not be the case in reality and may lead to an underestimation of the probability of extreme market movements.
- The use of a 10-day holding period assumes that all positions can be liquidated or hedged in 10 days. This does not fully capture the market risk arising from times of severe illiquidity, when a 10-day period may be insufficient to liquidate fully or hedge all positions.
- The use of a 99 per cent confidence level does not take account of any losses that might occur beyond this level of confidence.
- The use of historical data as a proxy for estimating future events may not encompass all potential events, particularly those which are extreme in nature.
- The assumption of independence between risk types may not always hold and therefore result in VAR not fully capturing market risk where correlation between variables is exhibited.
- VAR is calculated at the close of business with intra-day exposures not being subject to intra-day VAR calculations on a group basis.
- VAR does not necessarily capture all of the higher-order market risks and as such VAR may be underestimated.

The group recognises these limitations by augmenting the VAR limits with other position and sensitivity limit structures, as well as with stress testing both on individual portfolios and on a consolidated basis. The group's stress testing regime provides senior management with an assessment of the impact of extreme events on the market risk exposures of the group.

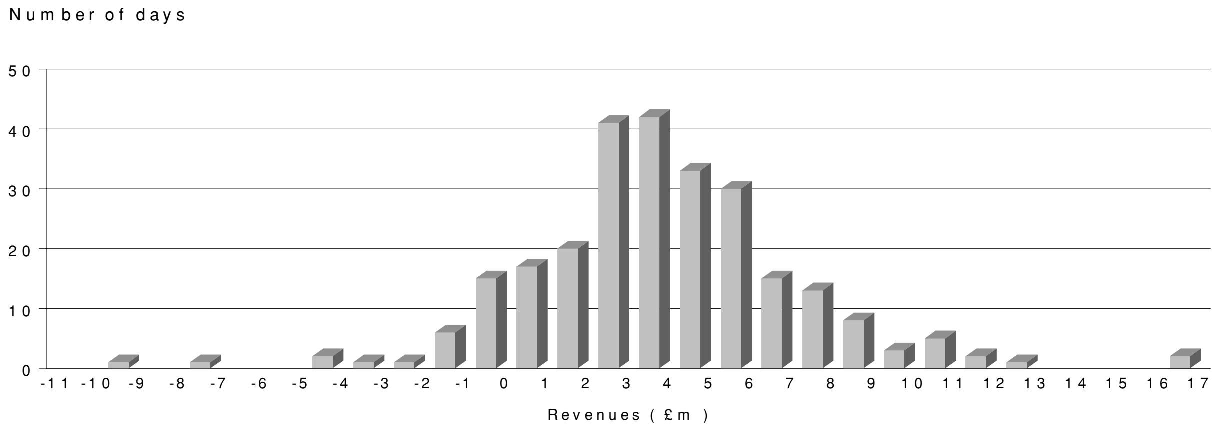
Trading VAR for 2002 is set out in the table below:

	At 31 December £m	**Minimum during the year £m**	**Maximum during the year £m**	**Average for the year £m**
Total trading activities	**25.5**	**17.0**	**41.9**	**28.1**
Foreign exchange trading positions	**7.0**	**3.5**	**22.4**	**9.9**
Interest rate trading positions	**22.9**	**15.9**	**36.4**	**22.7**
Equities trading positions	**3.8**	**0.8**	**5.3**	**2.1**

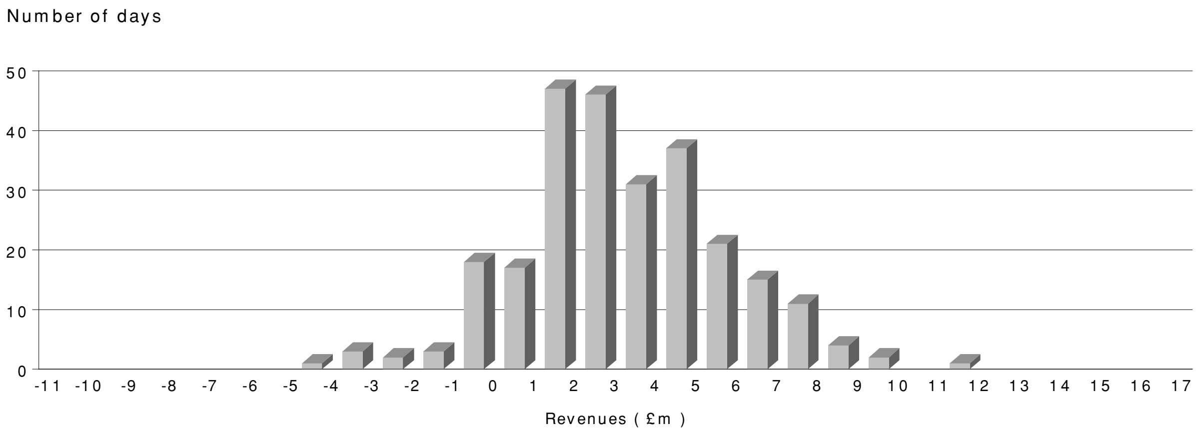
Trading VAR for 2001 is set out in the table below:

	At 31 December £m	Minimum during the year £m	Maximum during the year £m	Average for the year £m
Total trading activities	27.5	13.5	59.4	22.4
Foreign exchange trading positions	6.9	3.2	12.6	6.9
Interest rate trading positions	25.0	11.2	53.3	19.5
Equities trading positions	2.3	0.7	6.9	2.4

Daily distribution of market risk revenues in 2002



Daily distribution of market risk revenues in 2001



The average daily revenue earned from market-risk-related treasury activities in 2002, including accrual book net interest income and funding related to dealing positions, was £3.7 million, (2001: £3.1 million). The standard deviation of this daily revenue was £3.3 million (2001: £2.5 million). An analysis of the frequency distribution of daily revenues shows that negative revenues were reported on only 27 days during 2002. The most frequent result was a daily revenue of between £3 million and £4 million, with 42 occurrences. The highest daily revenue was £16.7 million.

Foreign exchange exposure

The group's foreign exchange exposure comprises trading exposures and structural foreign currency translation exposure.

Trading value at risk

The foreign exchange exposure comprises exposures that arise from foreign exchange dealing within the group's treasury centres and currency exposures originated by the group's banking businesses. The latter are transferred to local treasury units where they are managed together with exposures which result from dealing within approved limits. VAR on foreign exchange trading positions is shown in the table on the previous page.

Structural currency exposure

The bank's structural foreign currency exposure is represented by the net asset value of its foreign currency equity and subordinated debt investments in its branches, subsidiary undertakings, joint ventures and associates. Gains or losses on structural foreign currency exposures are taken to reserves.

The group's structural foreign currency exposures are managed with the primary objective of ensuring, where practical, that the group's and individual banking subsidiaries' tier 1 capital ratios are protected from the effect of changes in exchange rates. This is usually achieved by denominating tier 1 capital broadly in proportion to the corresponding foreign-currency-denominated risk-weighted assets at a subsidiary bank level. The group considers hedging structural foreign currency exposures only in limited circumstances, including protecting the tier 1 capital ratio or the value of capital invested. Such hedging would be undertaken using forward foreign exchange contracts or by financing with borrowings in the same currencies as the functional currencies involved.

As subsidiaries are generally able to balance adequately foreign currency tier 1 capital with foreign currency risk-weighted assets, the group's structural foreign currency exposures are usually unhedged, including exposures due to foreign-currency-denominated profits arising during the year. There were no material effects from foreign currency exchange rate movements on group or subsidiary tier 1 capital ratios during the year.

The main operating (or functional) currencies of the group's subsidiaries are sterling, euros, US dollars, Swiss francs, Hong Kong dollars, Turkish lira and Maltese liri.

Since the currency in which the group prepares its consolidated financial statements is sterling, the group's consolidated balance sheet is affected by movements in the exchange rates between these functional currencies and sterling. These currency exposures are referred to as structural foreign currency exposures. Translation gains and losses arising from these exposures are recognised in the statement of total consolidated recognised gains and losses.

Details of the group's structural foreign currency exposure can be found in Note 37 'Market risk management' in the Notes on the Accounts.

Interest rate exposures

The group's interest rate exposures comprise those originating in its treasury trading activities and structural interest rate exposures; both are managed under limits described above. Interest rate risk arises on both trading positions and accrual books. The interest rate risk on interest rate trading positions is set out in the trading VAR table on page 30.

Structural interest rate risk

Structural interest rate risk arises from the differing repricing characteristics of commercial banking assets and liabilities, including non-interest-bearing liabilities such as shareholders' funds and some current accounts. The bank and each major subsidiary undertaking assess the structural interest rate risks which arise in their businesses and either transfer such risks to their local treasury unit for management or transfer the risks to separate books managed by their local asset and liability committee ('ALCO'). ALCOs regularly monitor all such interest rate risk positions, subject to interest rate risk limits agreed with HSBC Holdings. In the course of managing interest rate risk, quantitative techniques and simulation models are used, where appropriate, to identify the potential net interest income and market value effects of these interest rate positions in different interest scenarios. The primary objective of such interest rate risk management is to limit potential adverse effects of interest rate movements on net interest income.

Equities exposure

The group's equities exposure arises from equities and equity derivatives transactions. Value at risk relating to equity trading positions is set out in the trading VAR table on page 30.

Liquidity Management

The bank's commercial banking operations generate a surplus of stable retail deposits over loans to its customers. Together with its capital resources, this surplus is placed with the treasury where the group's funding and liquidity is managed in three main sites: Treasury and Capital Markets in London, CCF in Paris and Private Banking in Geneva, reflecting the different local regulatory requirements. In addition, all sites operate within the HSBC Group's liquidity policy. This policy includes:

- Projecting cash flows by major currency and consideration of the level of liquid assets in relation thereto.
- Maintenance of strong balance sheet liquidity ratios.
- Monitoring of depositor concentration both in terms of the overall funding mix and to avoid undue reliance on large individual depositors.
- Maintenance of liquidity contingency plans.

Core retail deposits (current accounts and savings deposits payable on demand or at short notice) form a significant part of the group's overall funding. Considerable importance is attached to this core deposit base which, over the years, has been stable and predictable. The HSBC Group prefers to grow its balance sheet through increasing core retail deposits where possible.

Treasury and Capital Markets is an important player in the money and debt capital markets. As a leading market maker in loans and deposits, the bank routinely accepts deposits, often of a short-term nature, from banks and other institutions and makes advances to similar organisations. In addition, the funding of capital markets activities, by repo arrangements for example, will often result in funding directly in the wholesale market.

Approximately two thirds of the bank's asset base is sterling-based with the remainder mostly denominated in euros and US dollars. The non-sterling asset base is partially funded through currency-denominated capital issues and loan stock, supplemented by time deposits taken from the eurocurrency interbank market, from central banks, corporate customers and other financial institutions. The sources of such deposits, by type of institution and country, are monitored in order to avoid an undesirable dependence on any particular institution or category of depositor.

Treasury and Capital Markets in London has, for some years, operated a liquidity management policy based on consolidated net cash flows that conforms to the FSA's arrangements for the supervision of major UK banks' sterling liquidity. Central to these arrangements is the requirement for banks to be able to survive five working days without the renewal of any maturing net wholesale liabilities, and after the leakage of 5 per cent of the gross retail deposit base, for which purpose a minimum coverage ratio of specified liquid assets must be maintained. This ratio is computed daily, with the position being managed so as to exceed the minimum ratio. In addition to complying with these FSA requirements on sterling liquidity, the group also adopts the same consolidated cash flow methodology for managing its all-currency 0-5 working day liquidity exposures.

It is, however, the HSBC Group's policy that all professional deposits with residual maturities up to 30 days should be backed by liquid assets. This means that, in a crisis, the bank would be able to meet its obligations as they fall due for at least 30 days without recourse to the wholesale markets. This requirement is significantly more stringent than the regulatory requirement.

In France, CCF complies with the regulatory liquidity ratio requirements of the Banque de France, overseen and monitored by the Commission Bancaire. Banks are required to submit monthly returns which are used to compute a liquidity ratio as at the month end date, and quarterly returns which, in addition, include a future forecast of liquidity positions called 'observation ratios'. The ratios are derived by dividing liquid assets (which are subject to discount factors) by liabilities (which include a proportion of customer accounts, 5 per cent of off-balance-sheet commitments and all borrowings and subordinated loan stock maturing within one month). Banks are required to maintain, at all times, a ratio in excess of 100 per cent.

In Switzerland, Private Banking complies with the liquidity ratio requirements of the Swiss Federal Banking Commission. 'Liquidity I' applies to Swiss currency only and is calculated monthly, based on monthly averages. 'Liquidity II' embraces all currencies and requires that liquid and easily realisable assets are above one third of the difference between liabilities maturing within 30 days and realisable assets maturing within 30 days. This ratio is calculated daily.

Other non-UK units maintain sufficient liquidity to meet their day-to-day needs and local regulatory requirements unless specific arrangements are made for Treasury and Capital Markets in London to provide the necessary support. Both CCF and Private Banking are required to maintain high-quality liquid assets at least equal to 0-30 days' cumulative refinancing exposures on an all-currency basis for HSBC Group liquidity management purposes.

Financial Review (continued)

Operational Risk Management

Operational risk is the risk of loss arising through fraud, unauthorised activities, error, omission, inefficiency, systems failure or from external events. It is inherent to every business organisation and covers a wide spectrum of issues.

The HSBC Group manages this risk through a controls-based environment in which processes are documented, authorisation is independent and where transactions are reconciled and monitored. This is supported by an independent programme of periodic reviews, undertaken by internal audit and internal peer benchmarking studies, which ensure that the HSBC Group stays in line with best practice and takes account of lessons learned from publicised operational failures within the financial services industry. With effect from the beginning of 2001, operational risk losses are formally monitored quarterly. In each of the HSBC Group's subsidiaries local management is responsible for establishing an effective and efficient operational control environment in accordance with the HSBC Group's standards, so that its assets are adequately protected, and whereby the operational risks have been identified and adequate risk management procedures maintained to control those risks.

The HSBC Group maintains and tests contingency facilities to support operations in the event of disasters. Additional reviews and tests were conducted following the events of 11 September 2001 to incorporate lessons learned in the operational recovery from those circumstances. Insurance cover is arranged to mitigate potential losses associated with certain operational risk events.

Credit Risk Management

Credit risk is the risk that a customer or counterparty of the group will be unable or unwilling to meet a commitment into which it has entered with a member of the group. It arises from lending, trade finance, treasury and other activities. The group has in place standards, policies and procedures for the control and monitoring of all such risks.

HSBC Holdings is responsible for the formulation of high-level credit policies. It also reviews the application of the HSBC Group's universal facility grading system. The HSBC Group's credit risk limits to counterparties in the financial and government sectors are managed centrally to optimise the use of credit availability and to avoid excessive risk concentration. Cross-border risk is controlled through the imposition of country limits, with sub-limits by maturity and type of business. Transactions with counterparties in higher risk countries are considered on a case-by-case basis.

Within the overall framework of the HSBC Group policy, the bank has an established risk management process encompassing credit approvals, the control of exposures (including those to borrowers in financial difficulty), credit policy direction to business units and the monitoring and reporting of exposures both on an individual and a portfolio basis. Local management is responsible for the quality of its credit portfolios and follows a credit process involving delegated approval authorities and credit procedures, the objective of which is to build and maintain risk assets of high quality. Regular reviews are undertaken to assess and evaluate levels of risk concentration, including those to individual industry sectors and products.

Special attention is paid to the management of problem loans. Where deemed appropriate, specialist units are established to provide intensive management and control to maximise recoveries of doubtful debts.

Geographical concentrations of credit risk

The group restricts its exposure to the risk of payment difficulties arising with respect to individual countries and regions through a central HSBC Group system of internally determined country limits that relate to both economic and political risks. Exposures to individual countries and cross-border exposures in aggregate are kept under continuous review.

The following table shows total outstandings to counterparties in countries and regions which individually represent in excess of 5 per cent of total outstandings. Classification is based upon the country of residence of the borrower but recognises the transfer of country risk in respect of third party guarantees or residence of the head office where the borrower is a branch. In accordance with the Bank of England Country Exposure Report (Form C1) guidelines, outstandings comprise loans and advances (excluding settlement accounts), amounts receivable under finance leases, acceptances, commercial bills, certificates of deposit, and debt and equity securities (net of short positions), and exclude accrued interest and intra group exposures. Outstandings to counterparties in the United Kingdom, the bank's country of domicile, are not recorded on Form C1 and have therefore been computed on the basis of total group outstandings for classes of asset specified in the Form C1 guidelines, less amounts reported on Form C1.

As shown in the table below, the group's credit risk exposures are predominantly with countries and regions with developed economies. Outstandings to Latin America accounted for less than one per cent of total group assets.

Geographical analysis of outstandings	**2002** %	2001 %
United Kingdom	**45**	43
France	**18**	19
Germany	**7**	6
Rest of Continental Europe	**16**	16
Continental Europe	**41**	41
United States	**5**	7
Rest of world	**9**	9
	100	100

Concentrations of credit risk

Information relating to industry concentrations, gross of specific provisions, is given within Note 16 'Concentrations of exposure' in the Notes on the Accounts.

The group provides a diverse range of financial services both in the United Kingdom and internationally. As a result, its portfolio of financial instruments with credit risk is highly diversified with no exposures to individual industries or economic groupings totalling more than 10 per cent of consolidated total assets, except as follows:

- The bank's position as one of the principal UK clearing banks means that the group has a large concentration of credit risk in the United Kingdom. Within the United Kingdom, the group's credit risk is diversified over a wide range of industrial and economic groupings; and
- The group's position as part of a major international banking group means, that it has a significant concentration of exposure to banking counterparties. The majority of credit risk to the banking industry at 31 December 2002 and 31 December 2001 was concentrated in Europe (including the United Kingdom). Concentrations of credit risk arising from off-balance-sheet transactions are discussed in the section below on derivatives.

There are no special collateral requirements relating to industrial concentrations, with the exception of exposures to the property sector. The majority of exposures to the property and construction industry and the residential mortgage market are secured on the underlying property.

Derivatives

Off-balance-sheet financial instruments, commonly referred to as derivatives, are contracts the characteristics of which are derived from those of the underlying assets, interest and exchange rates or indices. They include futures, forwards, swap and options transactions in the foreign exchange, interest rate, equity and credit derivatives markets. Transactions are negotiated directly with customers, with the group acting as a counterparty, or can be dealt through exchanges.

Users of derivatives typically want to convert an unwanted risk generated by their business to a more acceptable risk, or cash. Derivatives provide an effective tool for companies to manage the financial risks associated with their business and, as a consequence, there has been a significant growth in derivatives transactions in recent years.

Financial Review (continued)

The group, through its dealing operations, acts as an intermediary between a broad range of users, structuring deals to produce risk management products to suit individual customer needs. As a result, the group can accumulate significant open positions in derivatives portfolios. These positions are managed constantly to ensure that they are within acceptable risk levels, with offsetting deals being undertaken to achieve this where necessary. As well as acting as a dealer, the group also uses derivatives (principally interest rate swaps) in the management of its own asset and liability portfolios and structural positions.

Risks associated with derivatives

Derivative instruments are subject to both market risk and credit risk.

The market risk associated with derivatives can be significant since large positions can be accumulated with a substantially smaller initial outlay than required in cash markets. Recognising this, only certain offices with sufficient derivative product expertise and appropriate control systems are authorised to trade derivative products. The management of market risk arising from derivatives business is monitored daily by the market risk control unit in each office and on a regular basis by Traded Markets Development and Risk, an independent unit within the Corporate, Investment Banking and Markets operation, in combination with market risks arising from on-balance-sheet instruments (Note 37 'Market risk management' in the Notes on the Accounts).

Unlike assets recorded on the balance sheet, where the credit risk is typically the full amount of the principal value, together with any unrealised interest accrued or mark-to-market gain ('Credit risk management' in the Financial Review on page 34), the credit risk relative to a derivative is principally the replacement cost of any contract with a positive mark-to-market gain and an estimate for the potential future change in value, reflecting the volatilities affecting the contract. Credit risk on contracts having a negative mark-to-market value is restricted to the potential future change in value. Credit risk on derivatives is, therefore, small in relation to a comparable balance sheet risk. In addition, credit exposure with individual counterparties can be reduced by the receipt of collateral and close-out netting agreements, which allow for positive and negative mark-to-market values on different transactions to be offset and settled by a single payment in the event of default by either party. Such agreements are enforceable in the jurisdictions of the major market makers and the group has executed close-out netting agreements with the majority of these counterparties, notwithstanding the fact that the group deals only with the most creditworthy counterparties.

To reduce credit risk, management may deem it necessary to obtain collateral. The amount and nature of the collateral obtained is based on management's credit evaluation of the customer. Collateral held varies but will generally be in the form of liquid securities.

The following table analyses the replacement cost of all third-party exchange rate, interest rate and equities contracts with positive mark-to-market gains, after netting where possible, by maturity and by category of counterparty at 31 December 2002 and 31 December 2001. The table shows that the replacement cost of derivatives is predominately with banks and under five years.

Replacement cost

	Residual maturity					
	Less than one year £m	One to five years £m	Over five years £m	Netting £m	**Total 2002 £m**	Total 2001 £m
Government	**3**	**34**	**73**	**(90)**	**20**	6
Banks	**4,385**	**6,852**	**3,398**	**(8,058)**	**6,577**	4,782
Non-bank financial institutions						
Exchanges*	**114**	**27**	**—**	**—**	**141**	22
Other	**945**	**1,154**	**450**	**(712)**	**1,837**	1,625
Other sectors	**676**	**465**	**144**	**(462)**	**823**	661
Total 2002	**6,123**	**8,532**	**4,065**	**(9,322)**	**9,398**	
Total 2001	4,508	5,392	1,762	(4,566)		7,096

** Exchanges with margining requirement*

The following table analyses the maturity profile of the contract amounts of third-party derivative contracts outstanding at 31 December 2002 and 31 December 2001. This shows that the majority of contracts are executed over the counter and mature within one year.

Contract amount	Residual maturity				
	Less than one year £m	One to five years £m	Over five years £m	Total **2002** **£m**	Total 2001 £m
Exchange rate, interest rate and equities contracts					
—exchanges with margining requirements	**49,341**	**22,378**	**4,195**	**75,914**	52,065
—other	**555,113**	**301,835**	**114,379**	**971,327**	931,104
Total 2002	**604,454**	**324,213**	**118,574**	**1,047,241**	
Total 2001	623,914	277,860	81,395		983,169

Further information on derivatives can be found in Note 35 'Financial instruments' in the Notes on the Accounts.

Derivatives used for trading purposes

Contracts for trading purposes are undertaken both for the group's own account and to service its corporate customer base, including designing structured products to meet the specific requirements of customers. Derivatives are used for trading purposes in order to generate income from customer-driven business and dealing income from market fluctuations.

Trading positions are valued on a mark-to-market basis.

In liquid portfolios, the market values are determined by reference to independently sourced mid-market prices where it is reasonable to assume the positions could be sold at that price. In those instances where markets are less liquid and/or where positions have been held for extended periods, portfolios will be valued by reference to bid or offer prices as appropriate.

In relation to certain products, such as over-the-counter derivative instruments, there are no independent prices quoted in the markets. In these circumstances market values are determined by reference to standard industry models, which typically utilise discounted cash flow techniques to derive the market value. The models may be in-house developed or software vendor packages.

In valuing transactions, prices may be amended in respect of those positions considered illiquid, having recognition of the size of the position vis à vis the normal market trading volumes in that product.

The main valuation sources are securities prices, foreign exchange rates, and interest rate yield curves.

The group's derivative transactions are predominantly in plain vanilla instruments, primarily comprising interest rate and foreign exchange contracts, where the marked to market values are readily determinable by reference to independent prices and valuation quotes, as described above.

There are a limited number of structured transactions which have been performed, primarily to meet specific customer demand, where standard industry models are not routinely available, and where there is no market quotation. For these products, the group has developed its own proprietary models for the purposes of performing valuations. These models are rigorously checked by Finance and Operations departments on an ongoing basis to ensure that the model assumptions are, and remain, valid over the transaction life, which is generally less than five years.

The average mark-to-market values for the years ended 31 December 2002 and 31 December 2001 are analysed in the following table. Positive amounts represent replacement cost values, while negative amounts represent current mark-to-market losses.

Average mark-to-market values	2002 £m	2001 £m
Exchange rate contracts		
Assets	**5,495**	5,209
Liabilities	**(5,700)**	(5,295)
Interest rate contracts		
Assets	**8,363**	5,947
Liabilities	**(8,442)**	(6,084)
Equities contracts		
Assets	**897**	813
Liabilities	**(1,011)**	(791)

Asset and liability balances arising from derivative contracts are not netted, except where a legal right of set-off exists.

Assets, including gains, resulting from derivatives that are marked to market, are included within 'Other assets' in the consolidated balance sheet (on page 60). Liabilities, including losses, resulting from such contracts, are included in 'Other liabilities'.

The contract amount, replacement cost and mark-to-market values of third party and internal trading derivatives by product type is shown on page 109, in Note 35 'Financial instruments' in the Notes on the Accounts.

Derivatives used for non-trading purposes

The majority of the transactions undertaken for non-trading purposes are between business units within the group, one of which is a trading desk, which may then lay off the resulting position by trading in the external market. Internal positions are integral to the group's asset and liability management.

Board of Directors

Directors

Sir John Bond, *Chairman*
Age 61. A Director since 1993 and Chairman from 1998. Group Chairman of HSBC Holdings plc. Joined HSBC in 1961. Chairman of HSBC USA Inc., HSBC Bank USA, HSBC Bank Canada and HSBC Bank Middle East. A Director of The Hongkong and Shanghai Banking Corporation Limited. Chairman of the Institute of International Finance, Inc and a Director of Ford Motor Company. A member of the Court of the Bank of England.

Sir Keith Whitson, *Deputy Chairman*
Age 59. A Director since 1992, Deputy Chief Executive from 1992 to 1994, Chief Executive from 1994 to 1998 and Deputy Chairman since 1998. Joined HSBC in 1961. Group Chief Executive of HSBC Holdings plc. Chairman of HSBC Bank A.S. and Deputy Chairman of the Supervisory Board of HSBC Trinkaus & Burkhardt KGaA. A Director of The Hongkong and Shanghai Banking Corporation Limited, HSBC USA Inc., HSBC Bank Canada and Grupo Financiero Bital, S.A. de C.V. A non-executive Director of the Financial Services Authority.

W R P Dalton, *Chief Executive*
Age 59. A Director and Chief Executive since 1998. An executive Director of HSBC Holdings plc. Joined HSBC in 1980. President and Chief Executive Officer, HSBC Bank Canada from 1992 to 1997. A Director of CCF S.A., HSBC Investment Bank Holdings plc and HSBC Private Banking Holdings (Suisse) SA. Vice-President of The Chartered Institute of Bankers. A non-executive Director of MasterCard International Inc. and a non-executive Director and Chairman of Young Enterprise.

D D J John, *Chief Operating Officer*
Age 52. A Director and Chief Operating Officer since January 2003. Joined HSBC in 1972. General Manager for Wales from 1993 to 1997. Chief Executive Officer, The Hongkong and Shanghai Banking Corporation Limited in India from 1997 to 1999. Deputy Chairman and Chief Executive of HSBC Bank Malaysia Berhad from 1999 to 2002. A Director of HSBC Bank Malta p.l.c.

C F W de Croisset
Age 59. A Director since 2000. Chairman and Chief Executive Officer of CCF S.A. An executive Director of HSBC Holdings plc. Joined CCF S.A. in 1980.

R Emerson*
Age 53. A Director since 1996. Senior Vice President Tax & Treasury at GlaxoSmithKline plc. Formerly a partner of Coopers & Lybrand.

C-H Filippi
Age 50. A Director since 2000. HSBC Holdings plc Group General Manager and Global Head of Corporate and Institutional Banking. Director of HSBC Investment Bank Holdings plc. Administrateur Directeur Général of CCF S.A. from 1998 to 2001. President of HSBC CCF Investment Bank (France) until 2001. Joined CCF S.A. in 1987.

S K Green
Age 54. A Director since 1995. Executive Director, Corporate, Investment Banking and Markets. Joined HSBC in 1982. An executive Director of HSBC Holdings plc. Group Treasurer, HSBC Holdings plc from 1992 to 1998. Chairman of HSBC Investment Bank Holdings plc and a Director of CCF S.A., HSBC Guyerzeller Bank AG, HSBC USA Inc., HSBC Bank USA, HSBC Private Banking Holdings (Suisse) SA and HSBC Trinkaus & Burkhardt KGaA.

C M S Jones*
Age 59. A Director since 2001. Chairman and Managing Director, James Beattie PLC.

A C Reed (Mrs)*
Age 46. A Director since 1996. Finance Director, Marks and Spencer Group plc.

H A Rose*
Age 62. A Director since 1997. Formerly Deputy Chairman of The Rover Group Limited.

J Singh*
Age 51. A Director since 2001. Chairman and Chief Executive Officer of Edwardian Group Limited. Member of the Board of Warwick Business School.

**Independent non-executive Director.*

Board of Directors (continued)

Secretary

I B Marshall
Age 53. Joined HSBC in 1995.

Registered Office: 8 Canada Square, London E14 5HQ

Senior Executives

A J Ashford
Age 53. General Manager, Personal Banking. Joined HSBC in 1979.

G P S Calvert, OBE
Age 50. General Manager, Northern Scotland and Northern Ireland Division. Joined HSBC in 1974.

I M Dorner
Age 48. General Manager, Northern, Scotland and Northern Ireland Division (designate). Joined HSBC in 1986.

R J Duke
Age 52. General Manager, Banking Services. Joined HSBC in 1971.

S T Gulliver
Age 43. Group General Manager and Head of Global Markets, Corporate, Investment Banking and Markets. Joined HSBC in 1980.

R P Hennessy
Age 49. Chief Financial Officer. Joined HSBC in 1982.

C Hothersall
Age 49. Chief Executive Officer, HSBC Bank Malta p.l.c. Joined HSBC in 1974.

A R F Hughes
Age 51. Chief Executive, First Direct. Joined HSBC in 1969.

A M Keir
Age 44. General Manager, Midlands Division. Joined HSBC in 1981.

A M Mahoney
Age 40. General Manager, Western and Wales Division. Joined HSBC in 1983.

R Morgan
Age 52. Head of Information Technology. Joined HSBC in 1980.

R J Moseley
Age 45. General Manager, Corporate, Investment Banking and Markets. Joined HSBC in 1976.

I D F Ogilvie
Age 43. Head of Human Resources (designate). Joined HSBC in 1981.

K Patel
Age 54. Group General Manager and Chairman, Global Investment Banking Division. Joined HSBC in 1984.

G E Picken
Age 53. General Manager, Commercial Banking. Joined HSBC in 1971.

J Ranaldi
Age 54. General Manager, Operations. Joined HSBC in 1982.

C S Smith
Age 56. Head of Credit and Risk. Joined HSBC in 1964.

R G Spence
Age 43. General Manager, Southern Division. Joined HSBC in 1978.

P E Stringham
Age 53. Group General Manager, Marketing. Joined HSBC in 2001.

C S O'N Wallis
Age 47. General Manager, International. Joined HSBC in 1978.

Report of the Directors

Results for 2002

The consolidated profit for the year attributable to the shareholders of the bank was £1,379 million.

A first interim dividend of £600 million was paid on the ordinary share capital during the year and the Directors have resolved to pay a second interim dividend for 2002 of £500 million.

Further information about the results is given in the consolidated profit and loss account on page 59.

Principal Activities and Business Review

The group provides a comprehensive range of banking and related financial services.

The bank has 1,633 branches in the United Kingdom. Outside the United Kingdom, it has branches in Australia, Belgium, the Czech Republic, France, Greece, Guernsey, the Hong Kong Special Administrative Region, Ireland, the Isle of Man, Israel, Italy, Jersey, the Netherlands, Spain and Sweden; it has representative offices in Argentina, Mexico, Singapore and Venezuela; and it has subsidiaries in Armenia, France, Germany, Greece, Kazakhstan, Malta, Russia, Spain, Switzerland and Turkey. Through these undertakings, the bank provides a comprehensive range of banking and related financial services.

In April 2002, HSBC Europe (Netherlands) BV, an indirect subsidiary of the bank, acquired 100 per cent of the interest in HSBC Republic Holdings (C.I.) Limited, HSBC International Trustee Limited, HSBC Republic Bank (Cyprus) Limited and HSBC Nominees Nassau Limited, from HSBC Investment Bank Holdings BV for a cash consideration of US$343 million (£221 million), as part of the ongoing reorganisation of the HSBC Group's private banking activities.

In July 2002, the bank acquired 100 per cent of HSBC Germany Holdings GmbH from HSBC Investment Bank Holdings BV, for a cash consideration of €549 million (£356 million). HSBC Germany Holdings GmbH holds the HSBC Group's 73.47 per cent interest in HSBC Trinkaus & Burkhardt KGaA.

In July 2002, HSBC Private Banking Holdings (Suisse) SA acquired 100 per cent of HSBC Republic Bank (UK) Limited from HSBC Investment Bank plc, for a consideration of £256 million, as part of the HSBC Group's continued restructuring of its private banking interests.

In September 2002, the bank acquired 100 per cent of Benkar Tuketici Finansmani ve Kart Hizmetleri A.S., to complement its existing operations in Turkey, for a cash consideration of up to US$75 million (£47 million).

On 30 November 2002, the investment banking activities of HSBC Investment Bank plc were transferred to the bank by means of a Private Act of Parliament 'The HSBC Investment Banking Act 2002'. The main objective of the transfer was to align corporate and investment banking, a key initiative of the HSBC Group.

The bank's obligation to file reports with the US Securities and Exchange Commission has been suspended, following, among other things, the re-listing of two issues of the bank's subordinated notes to London from New York. As a consequence, an *Annual Report on Form 20-F* has not been prepared.

A review of the development of the business of the group during the year and an indication of likely future developments are given in the Business Description and Financial Review on pages 4 to 38.

Share Capital

In March 2002, the bank redeemed at US$20 and US$5 per share respectively, all the non-cumulative Series 1 and 2 Second Dollar Preference Shares of US$0.01 each in issue. This redemption was funded by HSBC Holdings plc subscribing US$50,000,000 for 2,000,000 Series 2 Third Dollar Preference Shares of US$0.01 each.

In July 2002, HSBC Holdings plc subscribed the equivalent of £256,000,000 for one additional ordinary share of £1 credited as fully paid, in the ordinary share capital of the bank. The share was issued as part of the continued restructuring of the HSBC Group's private banking interests that commenced in December 2000.

In November 2002, HSBC Investment Bank plc subscribed the equivalent of £1,316,680 for 65,884 additional ordinary shares of £1 each credited as fully paid, in the ordinary share capital of the bank. These shares, which were issued in consideration for the transfer of the Madrid branch of HSBC Investment Bank plc, were transferred to HSBC Holdings plc on 11 December 2002.

Report of the Directors (continued)

Valuation of Freehold and Leasehold Land and Buildings

Freehold and long leasehold properties were revalued in September 2002 in accordance with the bank's policy of annual valuation. As a result of this revaluation, the net book value of land and buildings has decreased by £66 million. Further details are included in Note 23 'tangible fixed assets' in the Notes on the Accounts.

Board of Directors

The objectives of the management structures within the bank, headed by the Board of Directors and led by the Chairman, are to deliver sustainable value to shareholders. Implementation of the strategy set by the Board is delegated to the bank's Executive Committee under the leadership of the Chief Executive.

The Board meets regularly and Directors receive information between meetings about the activities of committees and developments in the bank's business. All Directors have full and timely access to all relevant information and may take independent professional advice if necessary.

The names of Directors serving at the date of this report and brief biographical particulars for each of them are set out on page 39.

D W Baker retired as Director and Chief Operating Officer on 31 December 2002 and D D J John was appointed Director and Chief Operating Officer with effect from 1 January 2003. Having been appointed since the last Annual General Meeting, D D J John will retire at the forthcoming Annual General Meeting and offer himself for election.

C F W de Croisset, R Emerson and C-H Filippi will retire by rotation at the forthcoming Annual General Meeting. With the exception of R Emerson, who will retire, they will offer themselves for re-election.

None of the Directors had, during the year or at the end of the year, a material interest, directly or indirectly, in any contract of significance with the bank or any of its subsidiary undertakings.

Board Committees

The Board has appointed a number of committees consisting of certain Directors and senior executives. The following are the principal committees:

Executive Committee

The Executive Committee meets regularly and operates as a general management committee under the direct authority of the Board. The members of the Executive Committee are W R P Dalton (Chairman), D D J John, both of whom are executive Directors, C-H Filippi, a Director, and A J Ashford, R J Duke, S T Gulliver, R P Hennessy, R J Moseley, K Patel, G E Picken and C S Smith, all of whom are senior executives.

Audit Committee

The Audit Committee meets regularly with the bank's senior financial, internal audit and compliance management and the external auditor to consider the bank's financial reporting, the nature and scope of audit reviews and the effectiveness of the systems of internal control and compliance. The members of the Audit Committee are H A Rose (Chairman), R Emerson and Mrs A C Reed, all of whom are independent non-executive Directors.

Property Committee

The Property Committee met regularly to supervise and control the development of the new Head Office building in London Docklands. The Committee was dissolved on 27 November 2002, following the completion and occupation of the new Head Office building. The members of the Committee were Sir Wilfrid Newton (Chairman), a former independent non-executive Director, W R P Dalton, D J Flint (Finance Director of HSBC Holdings plc), S K Green and Sir Keith Whitson.

Corporate Governance

The HSBC Group is committed to high standards of corporate governance. The bank has complied throughout the year with the relevant best practice provisions of the Combined Code on corporate governance appended to the Listing Rules of the Financial Services Authority.

The Directors are responsible for internal control in the group and for reviewing its effectiveness. Procedures have been designed for safeguarding assets against unauthorised use or disposition; for maintaining proper accounting records; and for the reliability of financial information used within the business or for publication. Such procedures are designed to manage rather than eliminate the risk of failure to achieve business objectives and can only provide reasonable and not absolute assurance against material errors, losses or fraud. The procedures also enable the bank to discharge its obligations under the Handbook of Rules and Guidance issued by the Financial Services Authority, the bank's lead regulator.

The key procedures that the Directors have established are designed to provide effective internal control within the HSBC Group and accord with the Internal Control Guidance for Directors on the Combined Code issued by the Institute of Chartered Accountants in England and Wales. Such procedures have been in place throughout the year and up to 3 March 2003, the date of approval of the *Annual Report and Accounts*. In the case of companies acquired during the year, the internal controls in place have been reviewed against the HSBC Group's benchmarks since the companies were acquired and they are being integrated into the HSBC Group's systems. The HSBC Group's key internal control procedures include the following:

- Authority to operate the bank is delegated to the Chief Executive who has responsibility for overseeing the establishment and maintenance of appropriate systems and controls and has authority to delegate such duties and responsibilities as he deems fit among the Directors and senior management. The appointment of executives to the most senior positions within the group requires the approval of the Board of Directors.
- Functional, operating, financial reporting and certain management reporting standards are established by HSBC Holdings' management for application across the whole HSBC Group. These are supplemented by operating standards set by the bank's management, as required.
- Systems and procedures are in place in the group to identify, control and report on the major risks including credit, changes in the market prices of financial instruments, liquidity, operational error, unauthorised activities and fraud. Exposure to these risks is monitored by the bank's or major subsidiaries' executive committees and the asset and liability management committees.
- Comprehensive annual financial plans are prepared, reviewed and approved by the Board of Directors. Results are monitored regularly and reports on progress as compared with the related plan are prepared monthly.
- Centralised functional control is exercised over all computer system developments and operations. Common systems are employed where possible for similar business processes. Credit and market risks are measured and reported on in the bank and major subsidiaries and aggregated for review of risk concentrations on an HSBC Group-wide basis.
- Responsibilities for financial performance against plans and for capital expenditure, credit exposures and market risk exposures are delegated with limits to line management. In addition, functional management in HSBC Holdings has been given responsibility to set policies, procedures and standards in the areas of: finance; legal and regulatory compliance; internal audit; human resources; credit; market risk; operational risk; computer systems and operations; property management; and for certain global product lines.
- Policies and procedures have been established to guide the bank, subsidiary companies and management at all levels in the conduct of business to avoid reputational risk which can arise from ethical, social or environmental issues, or as a consequence of operational risk events. As a banking group, the HSBC Group's good reputation depends upon the way in which it conducts its business but it can also be affected by the way in which clients, to which it provides financial services, conduct their business.
- The internal audit function, which is centrally controlled, monitors compliance with policies and standards and the effectiveness of internal control structures across the HSBC Group. The work of the internal audit function is focused on areas of greatest risk to the HSBC Group as determined by a risk management approach. The head of this function reports to the Group Chairman and the Group Audit Committee.

The Audit Committee has kept under review the effectiveness of this system of internal control and has reported regularly to the Board of Directors. The key processes used by the Committee in carrying out its reviews include regular reports from the heads of key risk functions; the production and regular updating of summaries of key controls measured against HSBC Group benchmarks which cover all internal controls, both financial and non-financial; annual confirmations from senior executives that there have been no material losses, contingencies or uncertainties caused by weaknesses in internal controls; internal audit reports; external audit reports; prudential reviews; and regulatory reports.

The Directors, through the Audit Committee, have conducted an annual review of the effectiveness of the bank's system of internal control covering all controls, including financial, operational and compliance and risk management.

Reputational, Strategic and Operational Risk

The HSBC Group regularly updates its policies and procedures for safeguarding against reputational, strategic and operational risks. This is an evolutionary process.

The safeguarding of the HSBC Group's reputation is of paramount importance to its continued prosperity and is the responsibility of every member of staff. The HSBC Group has always operated to the highest standards of conduct and, as a matter of routine, takes account of reputational risks to its business.

Reputational risks are considered and assessed by the Board, its committees and Senior Management in adherence with the HSBC Group standards. Standards on all major aspects of business are set for the HSBC Group and for individual subsidiary companies, businesses and functions. These policies, which form an integral part of the internal control systems, and which were strengthened considerably during 2002, are communicated through manuals and statements of policy and are promulgated through internal communications. The policies include environmental, ethical and social issues and set out operational procedures in all areas of reputational risk, including money laundering deterrence, environmental impact, anti-corruption measures and employee relations. The policy manuals address risk issues in detail, and co-operation between head office departments and businesses is required to ensure a strong adherence to the HSBC Group's risk management system and its corporate social responsibility practices.

Internal controls are an integral part of how the HSBC Group conducts its business. The HSBC Group's manuals and statements of policy are the foundation of these internal controls. There is a strong process in place to ensure controls operate effectively. Any significant failings are reported through the control mechanisms, internal audit and compliance functions to the Audit Committee, which keeps under review the effectiveness of the system of internal controls and reports regularly to the Board.

KPMG continues to assist the HSBC Group in developing systems to quantify the key direct environmental impact of its principal operations around the world. This third-party scrutiny of the environmental reporting system supports the HSBC Group's internal risk management procedures.

Health and Safety

The maintenance of appropriate health and safety standards throughout the bank remains a key responsibility of all managers and the bank is committed actively to managing all health and safety risks associated with its business. The bank's objectives are to identify, remove, reduce or control material risks of fires and of accidents or injuries to employees and visitors.

Health and Safety Policies, group standards and procedures are set by the Chief Executive and are implemented by line managers based in each location in which the bank operates.

Directors' Interests

According to the register of Directors' interests maintained by the bank pursuant to section 325 of the Companies Act 1985, the Directors of the bank at the year-end had the following beneficial interests in the shares and loan capital of HSBC Holdings:

Ordinary shares of US$0.50	At 1 January 2002	At 31 December 2002
D W Baker[1]	54,083	93,299
Sir John Bond[1]	273,841	274,369
C F W de Croisset[1]	34,170	35,664
W R P Dalton[1]	21,484	22,624
R Emerson	1,471	1,555
C-H Filippi[1]	385,870	275,870
S K Green[1]	127,804	173,608
Sir Keith Whitson[1]	121,484	121,687
11.69 per cent subordinated bonds 2002 of £1		
Sir John Bond	500,000	—[2]

1 *Details of additional interests in ordinary shares of US$0.50 each under the Share Option Plans and Restricted Share Plan are set out in the Directors' Remuneration Report on pages 54 to 56.*

2 *Redeemed on 31 July 2002.*

Sir John Bond has a personal interest in £290,000 of HSBC Capital Funding (Sterling 1) L.P. 8.208 per cent Non-cumulative Step-up Perpetual Preferred Securities, which he held throughout the year.

S K Green has a personal interest in €75,000 of HSBC Holdings plc 5½ per cent Subordinated Notes 2009 and in £100,000 of HSBC Bank plc 9 per cent Subordinated Notes 2005, which he held throughout the year.

As Directors of CCF S.A., C F W de Croisset, W R P Dalton, S K Green and C-H Filippi each have a personal interest in one share (reduced from ten to one following an amendment to the Company's articles of association, relating to the Directors' qualification shares) of €5 each in that company, which they held throughout the year. The Directors have waived their rights to receive dividends on these shares and undertaken on cessation of this directorship to transfer these shares to the bank.

Following the acquisition of CCF S.A. ('CCF') in 2000, HSBC Holdings ordinary shares of US$0.50 each were purchased by the HSBC Holdings General Employee Benefit Trust. These shares may be exchanged for CCF shares upon the exercise of CCF employee share options in the same ratio as the Exchange Offer for CCF (13 HSBC Holdings ordinary shares of US$0.50 each for each CCF share). As a potential beneficiary of the Trust, C F W de Croisset and C-H Filippi each have a technical interest in all of the shares held by the Trust. At 31 December 2002, the Trust held 35,745,555 HSBC Holdings plc ordinary shares of US$0.50 each.

Save as stated above, none of the Directors had an interest in any shares or debentures of HSBC Holdings or any of its subsidiary undertakings at the beginning or at the end of the year and none of the Directors, or members of their immediate families, was awarded or exercised any right to subscribe for any shares or debentures during the year.

Since the end of the year, the beneficial interests of Sir John Bond, W R P Dalton, S K Green and Sir Keith Whitson each increased by 19 HSBC Holdings ordinary shares of US$0.50 each, which were acquired by Computershare Trustees Limited using monthly contributions to the HSBC UK Share Ownership Plan. There have been no other changes in Directors' interests from 31 December 2002 to the date of this report.

Report of the Directors (continued)

Employee Involvement

The bank continues to regard communication with its employees as a key aspect of its policies and uses a wide variety of methods to encourage and maintain effective two-way communication with its employees on key issues including financial and economic factors which affect performance. Consultation arrangements include consultative forums for managers, agreed procedures with the recognised union and the bank's participation in an HSBC European Council. Every employee is encouraged to contribute to the success of the business through the performance management process and innovation. Improvement and creativity are encouraged and rewarded through 'Let's make a difference', the employee suggestion scheme. The involvement of employees in the performance of the bank is further encouraged through participation in bonus and share option plans as appropriate.

Many HSBC employees now participate in one or more of the HSBC Group's employee share plans. There are over 4,000 in the Share Ownership Plan and nearly 35,000 in Sharesave. Additionally, around 24,000 employees have discretionary options under the executive share option schemes.

Employment of Disabled Persons

The bank continues to be committed to providing equal opportunities to employees. The employment of disabled persons is included in this commitment and the recruitment, training, career development and promotion of disabled persons is based on the aptitudes and abilities of the individual. This is reinforced by the bank's adoption of the 'two tick' disability symbol. The bank's continued employment policy means that it will make every effort, if existing employees become disabled, to retain them within the workforce. The bank is a board member of the Employers' Forum on Disability.

The bank believes that good employment policies provide a firm foundation for the delivery of its services to the disabled community. Fifty four per cent of the bank's branches are now accessible to wheelchair users and this number continues to rise annually.

Community Involvement and Donations

During the year, the bank made charitable donations of £2.1 million, and made gifts in kind in support of community activities in the United Kingdom. Many staff also gave their time in voluntary activities for the benefit of others.

The bank continued to build its support for the communities in which it operates through activities focused on its commitment to education, particularly for under-privileged primary and secondary school students, and the environment. This commitment to education is led by Dame Mary Richardson, whose primary role within the HSBC Group is as Chief Executive of the HSBC Education Trust in the United Kingdom.

The Trust will consider charitable payments relating to education. Among the initiatives the Trust will support are increased funding for business and enterprise, sports and language colleges and primary and secondary school programmes for children in economically deprived areas.

The bank's staff and customers made contributions through a number of events and raised more than £600,000 for BBC Children in Need, being named one of the largest corporate fundraisers for that event. Staff raised a further £136,000 for the mobility charity Whizz-Kidz with sponsored walks, and £145,000 for research into women's cancers with Cancer Research UK's Race for Life.

In addition, the HSBC Group continued its policy of making donations to charities instead of sending Christmas cards. In 2002, this totalled £180,000, the beneficiaries being: SOS Children's Villages of India, running homes for abandoned children; Associaçao Maria Helen Drexel, a Brazilian children's home; St Raphael Centre for Aids in South Africa; The Treloar Trust, a school in Hampshire for disabled children; The Multiple Sclerosis Society; and The Eve Appeal, a gynaecology cancer research fund.

In 2002, the HSBC Group announced a major five year partnership 'Investing in Nature' with three charities: WWF; Botanic Gardens Conservation International; and Earthwatch under which US$50 million will be donated to fund conservation projects around the world. The 'Investing in Nature' programme will clean up three of the world's major rivers, benefiting 50 million people who depend upon them, help save 20,000 rare plant species from extinction and train 200 scientists and send 2,000 HSBC staff to work on vital conservation research projects worldwide.

No political donations were made during the year.

Supplier Payment Policy

The bank subscribes to the Better Payment Practice Code for all suppliers, the four principles of which are: to agree payment terms at the outset and stick to them; to explain payment procedures to suppliers; to pay bills in accordance with any contract agreed with the supplier or as required by law; and to tell suppliers without delay when an invoice is contested and settle disputes quickly.

Copies of, and information about, the Code are available from: Department of Trade and Industry, 1 Victoria Street, London SW1H 0ET.

The amount due to the bank's trade creditors at 31 December 2002 represented 25 days' average daily purchases of goods and services received from those creditors, calculated in accordance with the Companies Act 1985, as amended by Statutory Instrument 1997/571.

Auditor

KPMG Audit Plc has expressed its willingness to continue in office and the Board recommends that it be reappointed. A resolution proposing the reappointment of KPMG Audit Plc as auditor of the bank and giving authority to the Directors to determine its remuneration will be submitted to the forthcoming Annual General Meeting.

On behalf of the Board
I B Marshall, *Secretary*

3 March 2003

Directors' Remuneration Report

Remuneration Committee

The functions of the Remuneration Committee are fulfilled by the Remuneration Committee of the Board of the bank's parent company, HSBC Holdings plc. During 2002, the members of the Remuneration Committee were W K L Fung, Sir John Kemp-Welch, Lord Marshall and Sir Mark Moody-Stuart, all of whom were independent non-executive Directors of HSBC Holdings plc. Sir Mark Moody-Stuart succeeded Lord Marshall, who retired as a member of the Committee, as Chairman of the Committee on 1 January 2003.

The Remuneration Committee retains the services of Towers Perrin, a specialist remuneration consulting firm, which provides advice on executive pay issues. The Remuneration Committee also receives advice from the Group General Manager, Group Human Resources and the Senior Executive, Group Reward Management. Towers Perrin also provide other remuneration, actuarial and retirement consulting services to various parts of the HSBC Group. Other consultants are used from time to time to validate their findings.

Policy

In common with most businesses, the HSBC Group's performance depends on the quality and commitment of its people. Accordingly, the HSBC Group's stated strategy is to attract, retain and motivate the very best people.

In a business that is based on trust and relationships, the HSBC Group's broad policy is to look for people who want to make a long-term career with the organisation because trust and relationships are built over time.

Remuneration is an important component in people's decisions on which company to join, but it is not the only one; it is the HSBC Group's experience that people are attracted to an organisation with good values, fairness, the potential for success and the scope to develop a broad, interesting career.

The Remuneration Committee is responsible for determining the remuneration policy of HSBC Bank plc, including the terms of bonus plans, share option plans and other long-term incentive plans, and for agreeing the individual remuneration packages of the bank's executive Directors and other senior executives. No Directors are involved in deciding their own remuneration. During 2002, seven meetings of the Remuneration Committee were held.

The Remuneration Committee applies the following key principles:

- to pay against a market of comparative organisations;
- to offer fair and realistic salaries with an important element of variable pay based on relative performance;
- to have as many top-performers as possible at all levels within HSBC participating in some form of long-term share plan; and
- for new employees only, since 1996, to follow a policy of moving progressively from defined benefit to defined contribution Group pension schemes.

Basic salary and benefits

Salaries are reviewed annually in the context of individual and business performance, market practice, internal relativities and competitive market pressures. Allowances and benefits are largely determined by local market practice.

Annual performance-related payments

The level of performance-related variable pay depends upon the performance of the bank and the individual concerned. Key measures of success include achievement of financial goals, concerning both revenue generation and expense control; customer relationships; full utilisation of professional skills; and adherence to the HSBC Group's ethical standards. The HSBC Group has a long history of paying close attention to its customers in order to provide value for shareholders. This has been achieved by ensuring that the interests of the HSBC Group and its staff are aligned with those of its shareholders, and that the HSBC Group's approach to risk management serves the interests of all. Closer alignment with the interests of shareholders continues to be achieved through the promotion and extension of employee participation in the existing share plans and the bank's 'Let's Reward Success' initiative which seeks to incentivise all staff to deliver higher levels of customer-driven service.

Bonus ranges are reviewed in the context of prevailing market practice and overall remuneration.

Long-term share plans

In order to align the interests of staff with those of shareholders, share options are awarded to employees under the HSBC Holdings Group Share Option Plan and the HSBC Holdings savings-related share option plans.

The HSBC Holdings Restricted Share Plan 2000 is intended to align the interests of executives with those of shareholders by linking executive awards to the creation of superior shareholder value. This is achieved by focusing on predetermined targets. The shares awarded are normally held under restrictions for five years and are transferred to the individuals only after attainment of a performance condition which demonstrates the sustained and above average financial performance of the HSBC Group.

HSBC Holdings' executive Directors and Group General Managers have been eligible to receive conditional awards of Performance Shares under the HSBC Holdings Restricted Share Plan and the HSBC Holdings Restricted Share Plan 2000 since 1997. The award of Performance Shares under these plans was extended to other senior executives from 1999.

In appropriate circumstances, employees may receive awards under the HSBC Holdings Restricted Share Plan 2000 and the HSBC Holdings Group Share Option Plan. Participants in these Plans are also eligible to participate in the HSBC Holdings savings-related share option plans on the same terms as other eligible employees.

As part of the HSBC Group's strategy, the use of the existing share plans has been extended so that more employees participate in the success they help to create. The HSBC Holdings UK Share Ownership Plan enables employees to purchase HSBC Holdings shares from pre-tax salary.

Restricted Share Plan

The Remuneration Committee has proposed to the Trustee of the HSBC Holdings Restricted Share Plan 2000 that conditional awards of Performance Shares under the Plan should be made in 2003. The Trustee to the Plan will be provided with funds to acquire ordinary shares of US$0.50 each at an appropriate time after the announcement of the annual results. The 2003 awards proposed for Directors of the bank in respect of 2002 are:

	£000
Sir John Bond	1,100
W R P Dalton	750
S K Green	750
D D J John	250
	2,850

No share options will be granted under the HSBC Holdings Group Share Option Plan in respect of 2002 to the Directors listed above.

No award under the HSBC Holdings Restricted Share Plan 2000 will be made to C F W de Croisset or C-H Filippi in respect of 2002. They will instead receive awards of options to acquire 206,000 and 202,000 ordinary shares of US$0.50 each respectively under the HSBC Group Share Option Plan. Taking account of market practice in France, transitional arrangements will gradually align share option awards in CCF more closely with those elsewhere in the HSBC Group. In this respect, only 50 per cent of the above-mentioned awards will be subject to the same performance conditions set out below for the HSBC Holdings Restricted Share Plan 2000. Any future share option awards they may receive will be wholly subject to these performance conditions. In accordance with the arrangements agreed at the acquisition of CCF in 2000, the Group Share Option Plan awards made to Mr de Croisset and Mr Filippi in 2001 and 2002 were not subject to performance conditions.

The 1998 Restricted Share Plan awards were subject to performance conditions of earnings per share to be achieved in whole or in part, as follows:

- earnings per share in the year 2001 (the fourth year of the performance period) to be greater than earnings per share in 1997 (the base year for the calculation) by a factor equivalent to the composite rate of inflation (a weighted average of inflation in the UK, USA and the Hong Kong SAR) plus 2 per cent, compounded over each year of the performance period;
- earnings per share to increase relative to the previous year in not less than three of the four years of the performance period; and
- cumulative earnings per share over the four years of the performance period, 1998 to 2001 inclusive, must exceed an aggregate figure calculated by compounding 1997 earnings per share by a factor equivalent to the annual composite rate of inflation plus 2 per cent for each year of the performance period.

On meeting all of these three primary tests, 50 per cent of the conditional awards would be released to each eligible participant. A secondary test would apply such that, if the cumulative earnings per share over the performance period exceeded an aggregate figure calculated by compounding 1997 per share by a factor equivalent to the same annual composite rate of inflation as described above, plus 5 per cent or more, or 8 per cent or more, for each year of the performance period, 75 per cent or 100 per cent respectively of the conditional awards would be released.

Directors' Remuneration Report (continued)

In accordance with the rules of the Plan, as these tests were not satisfied over the years 1998 to 2001, the same tests are to be applied over the years 1999 to 2002. If the tests are not satisfied, the conditional share awards will be forfeited.

From 1999, the vesting of awards has been linked to the attainment of predetermined TSR targets as set out below.

Particulars of Directors' interests in shares held in the Restricted Share Plan are set out on page 56.

The HSBC Holdings Restricted Share Plan 2000

Purpose
The HSBC Holdings Restricted Share Plan 2000 is intended to reward the delivery of sustained financial growth of the HSBC Group. So as to align the interests of Directors and senior employees more closely with those of shareholders, the HSBC Holdings Restricted Share Plan 2000 links the vesting of 2003 awards to the attainment of predetermined total shareholder return ('TSR') targets.

TSR is defined as the growth in share value and declared dividend income during the relevant period. In calculating TSR, dividend income is assumed to be reinvested in the underlying shares.

Vesting schedule
Having regard to the HSBC Group's size and status within the financial sector, a benchmark has been established which takes account of:

1. a peer group of nine banks (ABN AMRO Holding N.V., Citigroup Inc., Deutsche Bank A.G., J. P. Morgan Chase & Co., Lloyds TSB Group plc, Oversea-Chinese Banking Corporation Limited, Mitsubishi Tokyo Financial Group Inc., Standard Chartered PLC, The Bank of East Asia, Limited) weighted by market capitalisation;

2. the five largest banks from each of the United States, the United Kingdom, continental Europe and the Far East, other than any within 1 above, weighted by market capitalisation; and

3. the banking sector of the Morgan Stanley Capital International World Index, excluding any within 1 and 2 above, weighted by market capitalisation.

By combining the above three elements and weighting the average so that 50 per cent is applied to 1, 25 per cent is applied to 2 and 25 per cent is applied to 3, an appropriate market comparator benchmark is determined.

The extent to which awards will vest will be determined by reference to the HSBC Group's TSR measured against the benchmark TSR. The calculation of the share price component within the HSBC Group's TSR will be the average market price over the 20 trading days commencing on the day when the annual results are announced, which in 2003 is 3 March. The starting point will be, therefore, the average over the period 3 to 28 March inclusive. TSR for the benchmark constituents will be based on their published share prices for 28 March 2003.

If the HSBC Group's TSR over the performance period exceeds the mean of the benchmark TSR, awards with a value, at the date of grant, of up to 100 per cent of earnings will vest. For higher value awards, the greater of 50 per cent of the award or the number of shares, equating at the date of grant to 100 per cent of earnings, will vest at this level of performance. If HSBC Holdings' TSR over the performance period places it within the upper quartile in the ranked list against the benchmark, these higher value awards will vest in full. For performance between the median and the upper quartile, vesting will be on a straightline basis.

The initial performance period will be three years. If the upper quartile performance target is achieved at the third anniversary of the date of grant, but not if it is achieved later, an additional award equal to 20 per cent of the initial performance share award will be made and will vest at the same time as the original award to which it relates. However, regardless of whether the upper quartile target is achieved on the third, fourth or fifth anniversary, full vesting and transfer of the shares will not generally occur until the fifth anniversary.

As a secondary condition, options and awards will only vest if the Remuneration Committee is satisfied that HSBC Holdings' financial performance has shown a sustained improvement in the period since the date of grant.

Awards will vest immediately in cases of death. The Remuneration Committee retains discretion to recommend early release of the shares to the Trustee in certain instances e.g. in the event of redundancy, retirement on grounds of injury or ill health, early retirement, retirement on or after contractual retirement or if the business is no longer part of the HSBC Group. Awards will normally be forfeited if the participant is dismissed or resigns from the HSBC Group.

Where events occur which cause the Remuneration Committee to consider that the performance condition has become unfair or impractical, the right is reserved to the Remuneration Committee to make such adjustments as in its absolute discretion it deems appropriate to make.

Service contracts and terms of appointment

Neither executive Director has a service contract with the bank or any of its subsidiaries with a notice period in excess of one year or with provisions for pre-determined compensation on termination which exceeds one year's salary and benefits in kind.

W R P Dalton is employed on a rolling contract, dated 5 January 1998, which requires 12 months' notice to be given by either party.

C F W de Croisset and C-H Filippi have contracts of employment that were in force before they joined the board of CCF S.A. In accordance with French legal requirements and practice, these contracts are suspended while they serve as executive Directors of CCF S.A. In the case of C-H Filippi, who ceased to be an executive Director of CCF S.A. in 2001, his contract remains suspended while he serves as an HSBC Group General Manager and will resume if he returns to employment with CCF S.A.

Senior executives are employed on service contracts which generally provide for a term of service expiring at the end of a period of up to two years, or the individual's sixtieth birthday, whichever is earlier.

Non-executive Directors are appointed for fixed terms not exceeding three years, subject to their re-election by shareholders at the subsequent Annual General Meeting. Independent non-executive Directors have no service contract and are not eligible to participate in the HSBC Group's share plans. Independent non-executive Directors' terms of appointment will expire in: 2003 — R Emerson; 2004 — H A Rose and J Singh; and 2005 — C M S Jones and Mrs A C Reed. None of the independent non-executive Directors will stand for re-election at the forthcoming Annual General Meeting.

Other Directorships

Executive Directors, if so authorised by the Board, may accept appointments as non-executive Directors of suitable companies which are not part of the HSBC Group. Executive Directors normally would be permitted to take on no more than one such appointment. Any remuneration receivable in respect of this appointment is paid to the bank, unless otherwise approved by the Remuneration Committee.

Directors' Remuneration Report (continued)

Audited Information

Directors' emoluments

The emoluments of the Directors of the bank for 2002 were as follows:

	Fees	Salary and other remuneration	Benefits in kind	Discretionary bonuses[1]	Total 2002	Total 2001
	£000	£000	£000	£000	£000	£000
Executive Directors						
D W Baker[2]	25	367[3]	1	347[4]	740	579
W R P Dalton[5]	—	566	26	—[6]	592	577
Non-executive Directors						
C F W de Croisset[5]	—	339	—	235	574	574
R Emerson	33	—	—	—	33	33
C-H Filippi	25	179	9	400[7]	613	532
C M S Jones	25	—	—	—	25	10
A C Reed	33	—	—	—	33	33
H A Rose	35	—	—	—	35	35
J Singh	25	—	—	—	25	23
Total	201	1,451	36	982	2,670	2,396

1 *These discretionary bonuses are in respect of 2002 and will be paid in 2003.*
2 *Retired as a Director and Chief Operating Officer on 31 December 2002, having reached normal retirement age on 30 September 2002.*
3 *Includes pension payments totalling £38,467 for the period 1 October to 31 December 2002.*
4 *Includes a long service award of £26,666.*
5 *W R P Dalton and C F W de Croisset receive a fee in respect of their directorship of HSBC Holdings plc. It is the HSBC Group policy that only one Directors' fee paid by the HSBC Group may be retained, therefore no fee is paid to them in respect of their directorship of HSBC Bank plc.*
6 *In return for the prior waiver of bonus, the employer contribution into the pension scheme has been increased by the amount of £400,000 (2001: £300,000) which would otherwise have been paid.*
7 *In return for the prior waiver of part of the bonus, the employer contribution into the pension scheme has been increased by the amount of £400,000 (2001: £280,000) which would otherwise have been paid.*

A fee of £25,000 (2001: £25,000) was paid to Sir Wilfrid Newton, a former Director of the bank, in respect of his role as Chairman of the Property Committee. Following the dissolution of this Committee, payment of the fee ceased with effect from 31 December 2002.

Sir John Bond, S K Green and Sir Keith Whitson received no emoluments from the bank or from its subsidiary undertakings.

Pensions

Pension arrangements for bank employees are provided by the HSBC Bank (UK) Pension Scheme, the assets of which are held in a separate trust fund. The Pension Scheme is administered by HSBC Bank Pension Trust (UK) Limited, whose Board of 19 Directors (eight of whom are elected by employees and one by pensioners) meets quarterly. It has three committees that monitor and review investment performance, discretionary benefits and administration and communications. The Pension Scheme does not invest in shares of the bank's parent company or in any of its subsidiary undertakings.

Pension arrangements to contractual retirement age of 60 for D W Baker are provided under the HSBC Bank (UK) Pension Scheme.

The pension arrangements for W R P Dalton to contractual retirement age of 60 are provided under the HSBC Holdings Overseas (No.1) Pension Plan on a defined contribution basis, with an employer contribution in respect of 2002 of £529,000 (including a bonus waiver of £400,000) (2001: £429,000 including a bonus waiver of £300,000).

Pension arrangements to contractual retirement age of 60 for C-H Filippi are provided under the HSBC Group International Contract Executive Retirement Plan on a defined contribution basis, with an employer contribution by way of bonus waiver in respect of 2002 of £400,000 (2001: £280,000).

C F W de Croisset and C-H Filippi are eligible for pension benefits which are supplementary to those accrued under the French State and compulsory arrangements. The amount of these supplementary pensions, payable from age 60, currently accrue at the rate of €6,098 and €4,574 per annum respectively for each year of service (maximum 18 years) as executive Directors of CCF S.A. In the case of C-H Filippi, these arrangements applied up to 30 June 2001, when he ceased to be an executive Director. The whole cost of these benefits is met by CCF S.A.

The pension entitlements earned by these Directors during the year are shown below:

	Accrued annual pension at 31 December 2002	Increase in accrued pension during 2002, excluding any increase for inflation	Transfer value of accrued pension at 1 January 2002 [1]	Transfer value of accrued pension at 31 December 2002 [1]	Change in transfer value of accrued pension 1 January – 31 December 2002 [1]
	£000	£000	£000	£000	£000
Executive Director					
D W Baker	— [2]	16	3,008	3,281 [2]	273
Non-executive Directors					
C F W de Croisset	56	7	516	626	110
C-H Filippi	14 [3]	—	92	83	(9)

1 *The transfer value represents a liability of the HSBC Group's pension funds and not a sum paid or due to the individual; it cannot therefore meaningfully be added to annual remuneration.*

2 *D W Baker retired, on attainment of normal retirement age, on 30 September 2002. He elected to commute £39,075 per annum from an immediate pension of £192,945 per annum, to provide a lump sum payment of £466,808. The transfer value of his benefits as at 31 December 2002 has been calculated by reference to the value of the pension in payment at that date plus the value of the lump sum payment, plus interest, to that date.*

3 *The accrued annual pension payable under the supplementary arrangements from CCF S.A., membership of which ceased on 30 June 2001, being the date he ceased to be an executive Director of CCF S.A.*

Only basic salary is pensionable. Neither of the executive Directors of the bank is subject to the earnings cap introduced by the 1989 Finance Act.

Pension payments totalling £384,000 (2001: £385,000) were made to seven (2001: seven) former Directors of the bank.

Directors' Remuneration Report (continued)

Audited Information

Share options

At 31 December 2002, the undernamed Directors held options to acquire the number of HSBC Holdings ordinary shares of US$0.50 each set against their respective names. The options were awarded for nil consideration at exercise prices equivalent to the market value at the date of award, except that options awarded under the HSBC Holdings savings-related share option plans since 2001 are exercisable at a 20 per cent discount to the market value at the date of award and those awarded before 2001 at a 15 per cent discount. There are no remaining performance criteria conditional upon which the outstanding options are exercisable. The market value of the ordinary shares at 31 December 2002 was £6.865. The highest and lowest market values of the ordinary shares during the year were £8.66 and £6.43. Market value is the mid-market price derived from the London Stock Exchange Daily Official List on the relevant date.

Options over ordinary shares of US$0.50 each

	Options held at 1 January 2002	Options awarded during year	Options exercised during year	Options held at 31 December 2002	Exercise price in £	Date of award	Exercisable from[1]	Exercisable until
Executive Directors								
D W Baker	21,000	—	—	21,000	5.0160	24 Mar 1997	24 Mar 2000	24 Mar 2007
	669[2]	—	669[3]	—	4.5206	9 Apr 1997	1 Aug 2002	31 Jan 2003
	24,000	—	—	24,000	6.2767	16 Mar 1998	16 Mar 2001	16 Mar 2008
	1,875[2]	—	1,167[4]	—[5]	5.3980	1 Apr 1999	1 Apr 2004	31 Jan 2005
	321[2]	—	135[4]	—[5]	6.7536	11 Apr 2001	1 Aug 2004	31 Jan 2005
W R P Dalton	22,704	—	—	22,704	2.4062	12 Oct 1993	12 Oct 1996	12 Oct 2003
	30,273	—	—	30,273	2.8376	8 Mar 1994	8 Mar 1997	8 Mar 2004
	36,000	—	—	36,000	2.1727	7 Mar 1995	7 Mar 1998	7 Mar 2005
	36,000	—	—	36,000[6]	3.3334	1 Apr 1996	1 Apr 1999	1 Apr 2006
	2,798	—	—	2,798[2]	6.0299	10 Apr 2000	1 Aug 2005	31 Jan 2006
Non-executive Directors								
Sir John Bond	75,000	—	—	75,000[6]	3.3334	1 Apr 1996	1 Apr 1999	1 Apr 2006
	2,798	—	—	2,798[2]	6.0299	10 Apr 2000	1 Aug 2005	31 Jan 2006
C F W de Croisset[7]	206,000	—	—	206,000	8.7120	23 Apr 2001	23 Apr 2004	23 Apr 2011
	—	206,000	—	206,000	8.4050	7 May 2002	7 May 2005	7 May 2012
C-H Filippi[7]	202,000	—	—	202,000	8.7120	23 Apr 2001	23 Apr 2004	23 Apr 2011
	—	202,000	—	202,000	7.4550	30 Aug 2002	30 Aug 2005	30 Aug 2012
S K Green	45,000[6]	—	45,000[8]	—	3.3334	1 Apr 1996	1 Apr 1999	1 Apr 2006
	2,498	—	—	2,498[2]	6.7536	11 Apr 2001	1 Aug 2006	31 Jan 2007
Sir Keith Whitson	60,000	—	—	60,000[6]	3.3334	1 Apr 1996	1 Apr 1999	1 Apr 2006
	2,798	—	—	2,798[2]	6.0299	10 Apr 2000	1 Aug 2005	31 Jan 2006

1 *May be advanced to an earlier date in certain circumstances, e.g. retirement.*
2 *Options awarded under the HSBC Holdings Savings-Related Share Option Plan.*
3 *At the date of exercise, 8 August 2002, the market value per share was £7.45.*
4 *At the date of exercise, 11 November 2002, the market value per share was £7.005.*
5 *Options over 708 and 186 shares lapsed on the partial exercise of the 1999 and 2001 awards respectively.*
6 *The exercise of these options was conditional upon the growth in earnings per share over a three-year period being equal to or greater than a composite rate of inflation (comprising 50 per cent of the Hong Kong Composite Consumer Price Index, 35 per cent of the UK Retail Price Index and 15 per cent of the USA All Urban Consumer Price Index) plus 2 per cent per annum. This condition has been satisfied.*
7 *Options awarded under the HSBC Holdings Group Share Option Plan. In accordance with agreements made at the time of the acquisition, there are no performance criteria conditional upon which the outstanding options are exercisable.*
8 *At the date of exercise, 13 March 2002, the market value per share was £8.34.*

Audited Information

At 31 December 2002, C F W de Croisset and C-H Filippi held the following options to acquire CCF shares of €5 each. On exercise of these options, each CCF share will be exchanged for 13 HSBC Holdings plc ordinary shares of US$0.50 each. The options were granted by CCF for nil consideration at a 5 per cent discount to the market value at the date of award. There are no performance criteria conditional upon which the outstanding options are exercisable.

Options over CCF S.A. shares of €5 each

Options held at 1 January 2002	Exercise price per share (€)	Options held at 31 December 2002	Equivalent HSBC Holdings ordinary shares of US$0.50 each at 31 December 2002	Date of award	Exercisable from	Exercisable until
C F W de Croisset						
10,000	32.78	10,000	130,000	23 Jun 1994	23 Jun 1996	23 Jun 2004
30,000	34.00	30,000	390,000	22 Jun 1995	22 Jun 1997	22 Jun 2005
30,000	35.52	30,000	390,000	9 May 1996	9 May 1998	9 May 2006
30,000	37.05	30,000	390,000	7 May 1997	7 Jun 2000	7 May 2007
30,000	73.50	30,000	390,000	29 Apr 1998	7 Jun 2000	29 Apr 2008
28,000	81.71	28,000	364,000	7 Apr 1999	7 Jun 2000	7 Apr 2009
28,000	142.50	28,000	364,000	12 Apr 2000	1 Jan 2002	12 Apr 2010
C-H Filippi						
20,000	73.50	20,000	260,000	29 Apr 1998	7 Jun 2000	29 Apr 2008
23,000	81.71	23,000	299,000	7 Apr 1999	7 Jun 2000	7 Apr 2009
23,000	142.50	23,000	299,000	12 Apr 2000	1 Jan 2002	12 Apr 2010

No options over CCF shares of €5 were awarded to either C F W de Croisset or C-H Filippi during the year.

Directors' Remuneration Report (continued)

Audited Information

Restricted Share Plan

HSBC Holdings Ordinary shares of US$0.50

	Awards held at 1 January 2002	Awards made during year	Monetary value of awards made during year £000	Awards vested during year	Awards held at 31 December 2002[1]	Date of award	Year in which awards may vest
D W Baker	18,451	3,348[2]	28	22,664	—	—	—
	26,025	—	—	23,388	3,773	10 Mar 2000	2005
	21,901	—	—	12,063	10,795	12 Mar 2001	2006
Sir John Bond	28,501	—	—	—	29,746	2 Mar 1998	2003
	55,353	10,045[2]	84	—	67,996	4 Mar 1999	2004
	81,791	—	—	—	85,365	10 Mar 2000	2005
	76,651	—	—	—	80,001	12 Mar 2001	2006
	—	114,779[3]	950	—	119,795	8 Mar 2002	2007
W R P Dalton	19,003	—	—	—	19,833	2 Mar 1998	2003
	32,290	5,859[2]	49	—	39,665	4 Mar 1999	2004
	37,178	—	—	—	38,803	10 Mar 2000	2005
	43,801	—	—	—	45,715	12 Mar 2001	2006
	—	72,492[3]	600	—	75,660	8 Mar 2002	2007
S K Green	22,799	—	—	—	23,796	2 Mar 1998	2003
	32,290	5,589[2]	49	—	39,665	4 Mar 1999	2004
	37,178	—	—	—	38,803	10 Mar 2000	2005
	76,651	—	—	—	80,001	12 Mar 2001	2006
	—	90,615[3]	750	—	94,575	8 Mar 2002	2007
Sir Keith Whitson	22,799	—	—	—	23,796	2 Mar 1998	2003
	46,128	8,371[2]	70	—	56,663	4 Mar 1999	2004
	52,049	—	—	—	54,323	10 Mar 2000	2005
	60,226	—	—	—	62,858	12 Mar 2001	2006
	—	90,615[3]	750	—	94,575	8 Mar 2002	2007

Unless otherwise indicated, vesting of these shares is subject to the performance tests described in the 'Report of the Directors' in the 1998, 1999, 2000 and 2001 Annual Report and Accounts respectively being satisfied.

1 *Includes additional shares arising from scrip dividends.*
2 *In accordance with the performance conditions over the three-year period to 31 December 2001 set out in the Annual Report and Accounts 1998, an additional award of 20 per cent of the initial performance share award was made on 7 May 2002. The market value per share on 7 May 2002 was £8.405. The shares acquired by the Trustee of the Plan were purchased at an average price of £8.13.*
3 *The market value per share on 8 March 2002 was £8.34. The shares acquired by the Trustee of the Plan were purchased at an average price of £8.28.*

On behalf of the Board
I B Marshall, *Secretary* 3 March 2003

Statement of Directors' Responsibilities in Relation to Financial Statements

The following statement, which should be read in conjunction with the Auditors' statement of their responsibilities set out in their report on the next page, is made with a view to distinguishing for shareholders the respective responsibilities of the Directors and of the Auditors in relation to the financial statements.

The Directors are required by the Companies Act 1985 to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the bank and its subsidiary undertakings as at the end of the financial year and of the profit or loss for the financial year. The Directors are required to prepare these financial statements on the going concern basis unless it is not appropriate. Since the Directors are satisfied that the group and the bank have the resources to continue in business for the foreseeable future, the financial statements continue to be prepared on the going concern basis.

The Directors consider that, in preparing the financial statements (on pages 59 to 122), the bank has used appropriate accounting policies, consistently applied, save as disclosed in the 'Notes on the Accounts', and supported by reasonable and prudent judgements and estimates, and that all accounting standards which they consider to be applicable have been followed.

The Directors have responsibility for ensuring that the bank keeps accounting records which disclose with reasonable accuracy, at any time, the financial position of the bank and which enable them to ensure that the financial statements comply with the Companies Act 1985.

The Directors have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the group and to prevent and detect fraud and other irregularities.

On behalf of the Board
I B Marshall, *Secretary*

3 March 2003

Independent Auditors' Report to the Members of HSBC Bank plc

We have audited the financial statements on pages 59 to 122.

This report is made solely to the bank's members in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the bank's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the bank and the bank's member for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and Auditors

The Directors are responsible for preparing the Directors' report and, as described on page 57, the financial statements in accordance with applicable United Kingdom law and accounting standards. Our responsibilities, as independent auditors, are established in the United Kingdom by statute, the Auditing Practices Board, the Listing Rules of the Financial Services Authority, and by our profession's ethical guidance.

We report to you our opinion as to whether the financial statements give a true and fair view and are properly prepared in accordance with the Companies Act 1985. We also report to you if, in our opinion, the Directors' report is not consistent with the financial statements, if the bank has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding Directors' remuneration and transactions with the group is not disclosed.

We read the other information accompanying the financial statements and consider whether it is consistent with those statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements.

Basis of audit opinion

We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion

In our opinion the financial statements give a true and fair view of the state of the affairs of the bank and the group as at 31 December 2002 and of the profit of the group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

KPMG Audit Plc 3 March 2003
Chartered Accountants
Registered Auditor
London

Consolidated Profit and Loss Account for the Year Ended 31 December 2002

	Note	2002 £m	2001* £m
Interest receivable			
— interest receivable and similar income arising from debt securities		**1,792**	2,021
— other interest receivable and similar income		**6,492**	7,462
Interest payable		**(4,245)**	(5,952)
Net interest income		**4,039**	3,531
Dividend income	*3*	**114**	33
Fees and commissions receivable		**3,161**	2,806
Fees and commissions payable		**(560)**	(460)
Dealing profits	*4*	**388**	442
Other operating income		**550**	626
Other income		**3,653**	3,447
Operating income		**7,692**	6,978
Administrative expenses	*5*	**(4,060)**	(3,682)
Depreciation and amortisation			
— tangible fixed assets	*23*	**(455)**	(437)
— goodwill	*22*	**(482)**	(460)
Operating expenses		**(4,997)**	(4,579)
Operating profit before provisions		**2,695**	2,399
Provisions			
— provisions for bad and doubtful debts	*15*	**(377)**	(308)
— provisions for contingent liabilities and commitments	*29*	**(27)**	(34)
Amounts written off fixed asset investments		**(146)**	(29)
Operating profit		**2,145**	2,028
Share of operating (loss)/profit in joint ventures and associates		**(4)**	29
Gains/(losses) on disposal of			
— interests in joint ventures and associates		**32**	166
— investments		**122**	58
— tangible fixed assets		**(10)**	9
Profit on ordinary activities before tax	*6*	**2,285**	2,290
Tax on profit on ordinary activities	*7*	**(808)**	(722)
Profit on ordinary activities after tax		**1,477**	1,568
Minority interests			
— equity		**(30)**	(28)
— non-equity		**(68)**	(70)
Profit for the financial year attributable to shareholders		**1,379**	1,470
Dividends (including amounts attributable to non-equity shareholders)	*9*	**(1,144)**	(1,563)
Retained profit/(loss) for the year		**235**	(93)
		pence	pence
Earnings per ordinary share (basic and diluted)	*10*	**167.5**	176.5

Movements in reserves are set out in Note 33 'Reserves'. All of the above represents continuing operations.

* *Figures for 2001 have been restated to reflect the adoption of Financial Reporting Standard 19, 'Deferred Tax', details of which are set out in Note 1(d) on the Accounts on page 64.*

Consolidated Balance Sheet at 31 December 2002

	Note	2002 £m	2001* £m
Assets			
Cash and balances at central banks		**1,834**	1,617
Items in the course of collection from other banks		**1,967**	2,249
Treasury bills and other eligible bills	*11*	**2,047**	2,937
Loans and advances to banks	*13*	**26,627**	32,331
Loans and advances to customers	*14*	**104,907**	89,001
Debt securities	*17*	**44,948**	41,877
Equity shares	*18*	**3,483**	2,287
Interests in joint ventures			
— gross assets		**137**	1,347
— gross liabilities		**(48)**	(1,183)
	19	**89**	164
Interests in associates	*20*	**109**	128
Intangible fixed assets	*22*	**8,338**	8,403
Tangible fixed assets	*23*	**4,790**	4,424
Other assets	*24*	**16,614**	14,463
Prepayments and accrued income		**2,625**	2,428
Total assets	*37*	**218,378**	202,309
Liabilities			
Deposits by banks	*25*	**24,399**	28,779
Customer accounts	*26*	**130,835**	118,886
Items in the course of transmission to other banks		**1,545**	1,439
Debt securities in issue	*27*	**8,343**	8,574
Other liabilities	*28*	**26,789**	19,683
Accruals and deferred income		**2,578**	2,165
Provisions for liabilities and charges	*29*		
— deferred taxation		**588**	537
— other provisions for liabilities and charges		**1,037**	758
Subordinated liabilities	*30*		
— undated loan capital		**1,374**	1,487
— dated loan capital		**2,856**	2,948
Minority interests			
— equity		**342**	244
— non-equity	*31*	**1,237**	1,161
Called up share capital	*32*	**797**	797
Share premium account	*33*	**12,208**	12,009
Revaluation reserves	*33*	**121**	166
Profit and loss account	*33*	**3,329**	2,676
Shareholders' funds (including non-equity interests)		**16,455**	15,648
Total liabilities	*37*	**218,378**	202,309
Memorandum items			
Contingent liabilities	*36*		
— acceptances and endorsements		**742**	846
— guarantees and assets pledged as collateral security		**14,359**	13,382
		15,101	14,228
Commitments	*36*	**61,377**	50,677

Sir John Bond, *Chairman*
W R P Dalton, *Chief Executive and Director*
D D J John, *Chief Operating Officer and Director*
I B Marshall, *Secretary*

* *Figures for 2001 have been restated to reflect the adoption of Financial Reporting Standard 19, 'Deferred Tax', details of which are set out in Note 1(d) on the Accounts on page 64.*

Balance Sheet of HSBC Bank plc at 31 December 2002

	Note	**2002** **£m**	2001* £m
Assets			
Cash and balances at central banks		**599**	727
Items in the course of collection from other banks		**1,558**	1,737
Treasury bills and other eligible bills	*11*	**1,430**	2,492
Loans and advances to banks	*13*	**14,224**	14,580
Loans and advances to customers	*14*	**76,207**	65,572
Debt securities	*17*	**20,589**	22,369
Equity shares	*18*	**1,209**	233
Interests in associates	*20*	**5**	7
Investments in subsidiary undertakings	*21*	**14,372**	13,688
Intangible fixed assets	*22*	**38**	40
Tangible fixed assets	*23*	**1,704**	1,560
Other assets	*24*	**7,716**	7,701
Prepayments and accrued income		**1,674**	1,997
Total assets	*37*	**141,325**	132,703
Liabilities			
Deposits by banks	*25*	**20,062**	21,631
Customer accounts	*26*	**79,770**	73,727
Items in the course of transmission to other banks		**1,063**	1,050
Debt securities in issue	*27*	**2,873**	3,583
Other liabilities	*28*	**14,604**	10,876
Accruals and deferred income		**1,230**	1,099
Provisions for liabilities and charges	*29*		
— deferred taxation		**60**	12
— other provisions for liabilities and charges		**313**	250
Subordinated liabilities	*30*		
— undated loan capital		**1,262**	1,369
— dated loan capital		**3,633**	3,458
Called up share capital	*32*	**797**	797
Share premium account	*33*	**12,208**	12,009
Revaluation reserves	*33*	**685**	789
Profit and loss account	*33*	**2,765**	2,053
Shareholders' funds (including non-equity interests)		**16,455**	15,648
Total liabilities	*37*	**141,325**	132,703
Memorandum items			
Contingent liabilities	*36*		
— acceptances and endorsements		**631**	810
— guarantees and assets pledged as collateral security		**8,423**	7,514
		9,054	8,324
Commitments	*36*	**50,469**	45,266

Sir John Bond, *Chairman*
W R P Dalton, *Chief Executive and Director*
D D J John, *Chief Operating Officer and Director*
I B Marshall, *Secretary*

* *Figures for 2001 have been restated to reflect the adoption of Financial Reporting Standard 19, 'Deferred Tax', details of which are set out in Note 1(d) on the Accounts on page 64.*

Statement of Total Consolidated Recognised Gains and Losses for the Year Ended 31 December 2002

	2002 £m	2001* £m
Profit for the financial year attributable to shareholders	**1,379**	1,470
Unrealised (deficit)/surplus on revaluation of land and buildings	**(44)**	64
Exchange and other movements	**359**	(126)
Total recognised gains and losses for the year	**1,694**	1,408
Prior period adjustment (as explained in Note 1(d))	**18**	
Total gains and losses since last annual report	**1,712**	

Reconciliation of Movements in Consolidated Shareholders' Funds for the Year Ended 31 December 2002

	2002 £m	2001* £m
Profit for the financial year attributable to shareholders	**1,379**	1,470
Dividends	**(1,144)**	(1,563)
	235	(93)
Other recognised gains and losses relating to the year	**315**	(62)
New share capital subscribed	**292**	1,503
Share capital redeemed	**(35)**	(573)
Net addition to shareholders' funds	**807**	775
Shareholders' funds at 1 January (originally £15,630 million at 31 December 2001 before adding prior period adjustment of £18 million)	**15,648**	14,873
Shareholders' funds at 31 December	**16,455**	15,648
Shareholders' funds are analysed as follows:		
Equity interests	**15,913**	15,048
Non-equity interests	**542**	600
	16,455	15,648

Non-equity interests in shareholders' funds comprise proceeds of the issue of US$ non-cumulative preference shares and the £ preferred ordinary share (Note 32), including share premium and after deducting unamortised issue costs.

No note of historical cost profits and losses has been presented as there is no material difference between the group's results as disclosed in the consolidated profit and loss account and the results on an unmodified historical cost basis.

* *Figures for 2001 have been restated to reflect the adoption of Financial Reporting Standard 19, 'Deferred Tax', details of which are set out in Note 1(d) on the Accounts on page 64.*

Notes on the Accounts

1 Basis of preparation

a The accounts have been prepared under the historical cost convention, as modified by the revaluation of certain investments and land and buildings and in accordance with applicable accounting standards.

The consolidated accounts are prepared in accordance with the special provisions of Part VII Chapter II of the Companies Act 1985 (‘the Act’) relating to banking groups.

As permitted by Section 230 of the Act, no profit and loss account is presented for the bank.

In accordance with Financial Reporting Standard (‘FRS’) 8, ‘Related Party Disclosures’, no disclosure is presented of transactions with entities that are part of the HSBC Group as all voting rights are controlled by HSBC Holdings plc which publishes its own publicly available accounts. The group has also taken advantage of the exemption under FRS 1 (revised), ‘Cash flow statements’, allowing wholly owned subsidiary undertakings to be excluded from the requirement to prepare a cash flow statement.

The group has adopted the provisions of FRS 19, ‘Deferred Tax’, with effect from 1 January 2002, and the transitional arrangements of FRS 17, ‘Retirement benefits’, which require additional disclosures only. For a discussion of the impact of the adoption of FRS 19 see Note 1(d) below.

The accounts have been prepared in accordance with the Statements of Recommended Practice (‘SORPs’) issued by the British Bankers’ Association (‘BBA’) and Irish Bankers’ Federation (‘IBF’) and with the SORP ‘Accounting issues in the asset finance and leasing industry’ issued by the Finance & Leasing Association (‘FLA’).

The SORP issued by the Association of British Insurers (‘ABI’), ‘Accounting for insurance business’ contains recommendations on accounting for insurance business for insurance companies and insurance groups. The group is primarily a banking group, rather than an insurance group, and, consistent with previously established practice for such groups preparing consolidated financial statements complying with Schedule 9 to the Act, values its long-term assurance businesses using the Embedded Value method. This method includes a prudent valuation of the discounted future earnings expected to emerge from business currently in force, taking into account factors such as recent experience and general economic conditions, together with the surplus retained in the long-term assurance funds.

b The preparation of financial information requires the use of estimates and assumptions about future conditions. This is particularly so in the development of provisions for bad and doubtful debts. Making reliable estimates of customers’ and other counterparties’ abilities to repay is often difficult even in periods of economic stability and becomes more difficult in periods of economic uncertainty such as exists in several of the group’s markets. Therefore, while management believes it has employed all available information to estimate adequate allowances for all identifiable risks in the current portfolios, there can be no assurance that the provisions for bad and doubtful debts or other provisions will prove adequate for all losses ultimately realised.

c The consolidated accounts of the group comprise the accounts of HSBC Bank plc (‘the bank’) and its subsidiary undertakings (together ‘the group’). Accounts of subsidiary undertakings are made up to 31 December. The consolidated accounts include the attributable share of the results and reserves of associated undertakings, based on accounts made up to dates not earlier than six months prior to 31 December.

All significant intra-group transactions are eliminated on consolidation.

Notes on the Accounts (continued)

1 Basis of preparation *(continued)*

d The adoption of FRS 19 has required a change in the method of accounting for deferred tax. Deferred tax is now recognised in full, subject to recoverability of deferred tax assets. Previously, deferred tax assets and liabilities were recognised only to the extent they were expected to crystallise. As deferred tax liabilities have generally been fully provided, the main impact of the change in method for the group has been the recognition of net deferred tax assets previously not recognised. The change in accounting policy has been reflected by way of a prior period adjustment. The comparative figures have been restated as follows:

Balance Sheet

group	*Intangible fixed assets — goodwill*	*Other assets*	*Provisions for liabilities and charges — deferred tax*	*Minority interests — equity*	*Profit and loss account reserve*
	£m	£m	£m	£m	£m
At 31 December 2001					
Under previous policy	8,436	14,457	583	243	2,658
Adoption of FRS 19	(33)	6	(46)	1	18
Under new policy	8,403	14,463	537	244	2,676

bank	*Investments in subsidiary undertakings*	*Provisions for liabilities and charges — deferred tax*	*Revaluation reserve*	*Profit and loss account reserve*
	£m	£m	£m	£m
At 31 December 2001				
Under previous policy	13,667	9	768	2,056
Adoption of FRS 19	21	3	21	(3)
Under new policy	13,688	12	789	2,053

Profit and Loss Account

group	2001 £m
Tax on profit on ordinary activities	
Under previous policy	(551)
Adoption of FRS 19	(171)
Under new policy	(722)

The impact of FRS 19 on the profit of the bank attributable to shareholders for 2001 was to reduce it from £1,873 million to £1,712 million.

The increase in the restated 2001 tax charge is due to the reversal of a benefit taken in 2001 in respect of deferred tax assets attributable under the old policy to prior years, and the establishment of a provision required under the new policy in respect of a possible clawback of capital allowances.

The effect on the results for the current period of the adoption of FRS 19 is immaterial.

2 Principal accounting policies

a *Income recognition*

Interest income is recognised in the profit and loss account as it accrues, except in the case of doubtful debts (Note 2b).

Fee and commission income is accounted for in the period when receivable, except where it is charged to cover the costs of a continuing service to, or risk borne for, the customer, or is interest in nature. In these cases, it is recognised on an appropriate basis over the relevant period.

b *Loans and advances and doubtful debts*

It is the HSBC Group's policy that each operating company will make provisions for bad and doubtful debts promptly where required and on a prudent and consistent basis.

Loans are designated as non-performing as soon as management has doubts as to the ultimate collectability of principal or interest, or when contractual payments of principal or interest are 90 days overdue. When a loan is designated as non-performing, interest will be suspended (see page 66) and a specific provision raised if required.

However, the suspension of interest may exceptionally be deferred for up to 12 months past due in the following situations:

— where cash collateral is held covering the total of principal and interest due and the right to set-off is legally sound; or

— where the value of net realisable tangible security is considered more than sufficient to cover the full repayment of all principal and interest due and credit approval has been given to the rolling-up or capitalisation of interest payments.

There are two basic types of provision, specific and general, each of which is considered in terms of the charge and the amount outstanding.

Specific provisions

Specific provisions represent the quantification of actual and expected losses from identified accounts and are deducted from loans and advances in the balance sheet.

Other than where provisions on smaller balance homogeneous loans are assessed on a portfolio basis, the amount of specific provision raised is assessed on a case-by-case basis. The amount of specific provision raised is the group's conservative estimate of the amount needed to reduce the carrying value of the asset to the expected ultimate net realisable value, and in reaching a decision consideration is given, among other things, to the following factors:

— the financial standing of the customer, including a realistic assessment of the likelihood of repayment of the loan within an acceptable period and the extent of the group's other commitments to the same customer;

— the realisable value of any security for the loan;

— the costs associated with obtaining repayment and realisation of the security; and

— if loans are not in local currency, the ability of the borrower to obtain the relevant foreign currency.

Where specific provisions are raised on a portfolio basis, the level of provisioning takes into account management's assessment of the portfolio's structure, past and expected credit losses, business and economic conditions, and any other relevant factors. The principal portfolios evaluated on a portfolio basis are credit cards and other consumer lending products.

Notes on the Accounts (continued)

2 Principal accounting policies *(continued)*

b *Loans and advances and doubtful debts (continued)*

General provisions

General provisions augment specific provisions and provide cover for loans that are impaired at the balance sheet date but which will not be identified as such until some time in the future. The HSBC Group requires operating companies to maintain a general provision, which is determined taking into account the structure and risk characteristics of each company's loan portfolio. Historic levels of latent risk are regularly reviewed by each operating company to determine that the level of general provisioning continues to be appropriate. Where entities operate in a significantly higher risk environment, an increased level of general provisioning will apply, taking into account local market conditions and economic and political factors. General provisions are deducted from loans and advances to customers in the balance sheet.

Loans on which interest is being suspended

Provided that there is a realistic prospect of interest being paid at some future date, interest on non-performing loans is charged to the customer's account. However, the interest is not credited to the profit and loss account but to an interest suspense account in the balance sheet, which is netted against the relevant loan. On receipt of cash (other than from the realisation of security), suspended interest is recovered and taken to the profit and loss account. A specific provision of the same amount as the interest receipt is then raised against the principal balance. Amounts received from the realisation of security are applied to the repayment of outstanding indebtedness, with any surplus used to recover any specific provisions and then suspended interest.

Non-accrual loans

Where the probability of receiving interest payments is remote, interest is no longer accrued and any suspended interest balance is written off.

Loans are not reclassified as accruing until interest and principal payments are up to date and future payments are reasonably assured.

Loan write offs

Loans and suspended interest are written off, either partially or in full, when there is no prospect of recovery of these amounts.

Assets acquired in exchange for advances

Assets acquired in exchange for advances in order to achieve an orderly realisation continue to be reported as advances. The asset acquired is recorded at the carrying value of the advance disposed of at the date of the exchange and provisions are based on any subsequent deterioration in its value.

c *Treasury bills, debt securities and equity shares*

Treasury bills, debt securities and equity shares intended to be held on a continuing basis are disclosed as investment securities and are included in the balance sheet at cost less provision for any permanent diminution in value.

Where dated investment securities have been purchased at a premium or discount, these premiums and discounts are amortised through the profit and loss account over the period from the date of purchase to the date of maturity so as to give a constant rate of return. If the date of maturity is at the borrower's option within a specified range of years, the maturity date that gives the most conservative result is adopted. These securities are included in the balance sheet at cost adjusted for the amortisation of premiums and discounts arising on acquisition. The amortisation of premiums and discounts is included in 'Interest receivable'. Any profit or loss on realisation of these securities is recognised in the profit and loss account as it arises and included in 'Gains on disposal of investments'.

2 Principal accounting policies *(continued)*

c *Treasury bills, debt securities and equity shares (continued)*

Other treasury bills, debt securities, equity shares and short positions in securities are included in the balance sheet at market value. Changes in the market value of such assets and liabilities are recognised in the profit and loss account as ‘Dealing profits’ as they arise. For liquid portfolios, market values are determined by reference to independently sourced mid-market prices. In certain less liquid portfolios, securities are valued by reference to bid or offer prices as appropriate. Where independent prices are not available, market values may be determined by discounting the expected future cash flows using an appropriate interest rate adjusted for the credit risk of the counterparty. In addition, adjustments are made for illiquid positions where appropriate.

Where securities are sold subject to a commitment to repurchase them at a predetermined price, they remain on the balance sheet and a liability is recorded in respect of the consideration received. Conversely, securities purchased under analogous commitments to resell are not recognised on the balance sheet and the consideration paid is recorded in ‘Loans and advances to banks’ or ‘Loans and advances to customers’.

d *Subsidiary undertakings, joint ventures and associates*

The bank’s investments in subsidiary undertakings are stated at net asset values including attributable goodwill, where this has been capitalised, with the exception of the group’s interest in long-term assurance business as explained in Note 2(g). Changes in net assets of subsidiary undertakings are accounted for as movements in the revaluation reserve.

Interests in joint ventures are stated at the group’s share of gross assets, including attributable goodwill, less the group’s share of gross liabilities.

Interests in associates are stated at the group’s share of net assets, including attributable goodwill.

Goodwill arises on the acquisition of subsidiary undertakings, joint ventures or associates when the cost of acquisition exceeds the fair value of the group’s share of separable net assets acquired. Negative goodwill arises on the acquisition of subsidiary undertakings, joint ventures and associates when the fair value of the group’s share of separable net assets acquired exceeds the cost of acquisition. For acquisitions made on or after 1 January 1998, goodwill is included in the balance sheet in ‘Intangible fixed assets’ in respect of subsidiary undertakings, in ‘Interests in joint ventures’ in respect of joint ventures and in ‘Interests in associates’ in respect of associates. Capitalised goodwill is amortised over its estimated life on a straight-line basis. For acquisitions prior to 1 January 1998, goodwill was charged against reserves in the year of acquisition. Capitalised goodwill is tested for impairment when necessary by comparing the present value of the expected future cash flows from an entity with the carrying value of its net assets, including attributable goodwill. Negative goodwill is credited in the profit and loss account in the periods expected to be benefited.

At the date of disposal of subsidiary undertakings, joint ventures or associates, any unamortised goodwill, or goodwill charged directly to reserves, is included in the group’s share of net assets of the undertaking in the calculation of the gain or loss on disposal of the undertaking.

e *Tangible fixed assets*

Land and buildings are stated at valuation or cost less depreciation, calculated to write off the assets over their estimated useful lives as follows:

— freehold land and land held on leases with more than 50 years to expiry are not depreciated;

— land held on leases with 50 years or less to expiry is depreciated over the unexpired terms of the leases; and

— buildings and improvements thereto are depreciated on cost or valuation at the greater of 2 per cent per annum on the straight-line basis or over the unexpired terms of the leases or over the remaining useful lives.

Equipment, fixtures and fittings are stated at cost less depreciation calculated on the straight-line basis to write off the assets over their estimated useful lives, which are generally between five and 20 years.

Operating lease assets (Note 2f) are depreciated over their useful economic lives such that, for each asset, rentals less depreciation are recognised at a constant periodic rate of return on the net cash invested in that asset.

Notes on the Accounts (continued)

2 Principal accounting policies *(continued)*

f *Finance and operating leases*

Assets leased to customers under agreements that transfer substantially all the risks and rewards associated with ownership, other than legal title, are classified as finance leases. Where the group is a lessor under finance leases, the amounts due under the lease, and under hire purchase contracts that are in the nature of finance leases, after deduction of unearned charges, are included in 'Loans and advances to banks' or 'Loans and advances to customers'. Finance charges receivable are recognised over the periods of the leases so as to give a constant rate of return on the net cash investment in the leases, taking into account tax payments and receipts associated with the leases.

Where the group is a lessee under finance leases, the leased assets are capitalised and included in 'Equipment, fixtures and fittings' and the corresponding liability to the lessor is included in 'Other liabilities'. Finance charges payable are recognised over the periods of the leases, based on the interest rates implicit in the leases.

All other leases are classified as operating leases and, where the group is the lessor, are included in 'Tangible fixed assets'. The residual values of equipment on operating leases are regularly monitored. Provision is made to the extent that the carrying value of equipment is impaired through residual values not being fully recoverable. Rentals payable and receivable under operating leases are accounted for on the straight-line basis over the periods of the leases and are included in 'Administrative expenses' and 'Other operating income' respectively.

g *Long-term assurance business*

The value placed on the group's interest in long-term assurance business includes a prudent valuation of the discounted future earnings expected to emerge from business currently in force, taking into account factors such as recent experience and general economic conditions, together with the surplus retained in the long-term assurance funds. These are determined annually in consultation with independent actuaries and are included in 'Other assets'.

Changes in the value placed on the group's interest in long-term assurance business are calculated on a post-tax basis and reported in the profit and loss account as part of 'Other operating income' after adjusting for taxation.

Long-term assurance assets and liabilities attributable to policyholders are recognised in the group's accounts in 'Other assets' and 'Other liabilities'.

h *Deferred taxation*

Deferred tax is recognised in full on timing differences between the accounting and taxation treatment of income and expenditure, subject to assessment of the recoverability of deferred tax assets. Deferred tax balances are not discounted.

i *Pension and other post-retirement benefits*

The group operates a number of pension and other post-retirement benefit schemes.

For UK defined benefit pension schemes, annual contributions are made, on the advice of qualified actuaries, for funding of retirement benefits in order to build up reserves for each scheme member during the employee's working life and used to pay a pension to the employee or dependant after retirement. The costs of providing these benefits are charged to the profit and loss account on a regular basis.

Arrangements for staff retirement benefits in overseas locations vary from country to country and are made in accordance with local regulations and custom. The pension cost of the major overseas schemes is assessed in accordance with the advice of qualified actuaries so as to recognise the cost of pensions on a systematic basis over employees' service lives.

The cost of providing post-retirement health-care benefits, which is assessed in accordance with the advice of qualified actuaries, is recognised on a systematic basis over employees' service lives.

2 Principal accounting policies *(continued)*

j *Foreign currencies*

Assets and liabilities denominated in foreign currencies are translated into sterling at the rates of exchange ruling at the year-end. The results of overseas branches and subsidiary undertakings, joint ventures and associates are translated into sterling at the average rates of exchange for the year.

Exchange differences arising from the retranslation of opening foreign currency net investments and the related cost of hedging and exchange differences arising from retranslation of the result for the year from the average rate to the exchange rate ruling at the year-end are accounted for in reserves.

Other exchange differences are recognised in the profit and loss account.

k *Off-balance-sheet financial instruments*

Off-balance-sheet financial instruments arise from futures, forward, swap and option transactions undertaken by the group in the foreign exchange, interest rate, equity and credit derivative markets. Netting is applied where a legal right of set-off exists. Mark-to-market assets and liabilities are presented gross, with netting shown separately.

Accounting for these instruments is dependent upon whether the transactions are undertaken for trading or non-trading purposes.

Trading transactions

Trading transactions include transactions undertaken for market-making, to service customers' needs and for proprietary purposes, as well as any related hedges.

Transactions undertaken for trading purposes are marked to market and the net present value of any gain or loss arising is recognised in the profit and loss account as 'Dealing profits', after appropriate deferrals for unearned credit margin and future servicing costs. Off-balance-sheet trading transactions are valued by reference to an independent liquid mid-market price where this is available. For those transactions where there are no readily quoted prices, which predominately relates to over the counter transactions, market values are determined by reference to independently sourced rates, using valuation models. Adjustments are made for illiquid positions where appropriate.

Assets, including gains, resulting from off-balance-sheet exchange rate, interest rate, equities and credit derivative contracts that are marked to market are included in 'Other assets'. Liabilities, including losses, resulting from such contracts, are included in 'Other liabilities'.

Non-trading transactions

Non-trading transactions are those that are held for hedging purposes as part of the group's risk management strategy against assets, liabilities, positions or cash flows measured on an accruals basis. Non-trading transactions include qualifying hedges and positions that synthetically alter the characteristics of specified financial instruments.

Non-trading transactions are accounted for on an equivalent basis to the underlying assets, liabilities or net positions. Any profit or loss arising is recognised on the same basis as that arising from the related assets, liabilities or positions.

To qualify as a hedge, the derivative must effectively reduce the price or interest rate risk of the asset, liability or anticipated transaction to which it is linked and be designated as a hedge at inception of the derivative contract. Accordingly, changes in the market value of the derivative must be highly correlated with changes in the market value of the underlying hedged item at inception of the hedge and over the life of the hedge contract. If these criteria are met, the derivative is accounted for on the same basis as the underlying hedged item. Derivatives used for hedging purposes include swaps, forwards and futures.

Notes on the Accounts (continued)

2 Principal accounting policies *(continued)*

k *Off-balance-sheet financial instruments (continued)*

Interest rate swaps are also used to alter synthetically the interest rate characteristics of financial instruments. In order to qualify for synthetic alteration, a derivative instrument must: be linked to specific individual, or pools of similar, assets or liabilities by the notional principal and interest rate risks of the associated instruments; and must achieve a result that is consistent with defined risk management objectives. If these criteria are met, accruals based accounting is applied, i.e. income or expense is recognised and accrued to the next settlement date in accordance with the contractual terms of the agreement.

Any gain or loss arising on the termination of a qualifying derivative is deferred and amortised to earnings over the original life of the terminated contract. Where the underlying asset, liability or position is sold or terminated, the qualifying derivative is immediately marked to market and any profit or loss arising is taken to the profit and loss account.

3 Dividend income

	2002	2001
	£m	£m
Income from equity shares	**114**	33

4 Dealing profits

	2002	2001
	£m	£m
Foreign exchange	**357**	321
Interest rate derivatives	**5**	41
Debt securities	**37**	39
Equities and other trading	**(11)**	41
	388	442

5 Administrative expenses

a *Analysis of expenses*

	2002	2001
	£m	£m
Staff costs		
— wages and salaries	**2,044**	1,899
— social security costs	**267**	244
— other pension costs (Note 5b below)	**196**	191
	2,507	2,334
Premises and equipment (excluding depreciation)	**545**	466
Other administrative expenses	**1,008**	882
	4,060	3,682

5 Administrative expenses *(continued)*

a *Analysis of expenses (continued)*

The average number of persons employed by the group during the year was made up as follows:

	2002	2001
UK Personal, Commercial, Corporate and Institutional Banking	**47,752**	49,110
UK Treasury and Capital Markets	**939**	944
Investment Banking	**156**	—
International Banking	**6,352**	4,542
CCF	**14,185**	13,391
Private Banking	**2,835**	1,561
HSBC Trinkaus & Burkhardt	**630**	—
	72,849	69,548

The average numbers of persons for acquisitions and transfers have been weighted in proportion to the time that they have been owned by the group.

b *Retirement benefits*

The group has continued to account for pensions in accordance with Statement of Standard Accounting Practice ('SSAP') 24, 'Accounting for pension costs' and the disclosures given in i) are those required by that standard. FRS 17, 'Retirement benefits' was issued in November 2000. Prior to full implementation, which has been deferred until accounting periods beginning on or after 1 January 2005, phased transitional disclosures are required from 31 December 2001. These disclosures, to the extent not given in i), are set out in ii).

i *Pension schemes*

Within the group, the HSBC Bank (UK) Pension Scheme, assets of which are held in a separate trust fund, covers 96 per cent of UK employees. The HSBC Bank (UK) Pension Scheme comprises a funded defined benefit scheme ('the Principal Scheme') and a defined contribution scheme which was established on 1 July 1996 for new employees.

Actuarial valuations of the assets and liabilities of the Principal Scheme are carried out triennially by professionally qualified actuaries to determine its financial position and to enable the bank to determine the level of contributions to be made to the Principal Scheme.

The actuarial valuation as at 31 December 2002 is currently in the course of preparation based on the circumstances as at that date. The latest valuation of the Principal Scheme was made at 31 December 1999 by C G Singer, Fellow of the Institute of Actuaries, of Watson Wyatt Partners. At that date, the market value of the Principal Scheme's assets was £7,265 million. The actuarial value of the assets represented 104 per cent of the benefits accrued to members, after allowing for expected future increases in earnings, and the resulting surplus amounted to £232 million. The method adopted for this valuation was the projected unit method and the main assumptions used were a long-term investment return of 6.85 per cent per annum, salary increases of 4.0 per cent per annum, equity dividend increases and rental growth of 3.5 per cent per annum, and post-retirement pension increases of 2.5 per cent per annum.

Following an interim review, the bank decided to increase contributions from 16.9 per cent to 20.0 per cent of pensionable salaries with effect from 1 August 2002, until completion of the actuarial valuation as at 31 December 2002.

The HSBC Group has given preliminary consideration to its funding strategy. The funding policy itself is reviewed on a systematic basis in consultation with the independent Scheme Actuary in order to ensure that the funding contributions from the sponsoring employers are appropriate to meet the liabilities of the Scheme over the long term. Full valuation calculations are currently in hand but the HSBC Group anticipates there will be a shortfall of at least £500 million on the funding basis which will be adopted for the Scheme. The HSBC Group has therefore decided to pay this amount into the Scheme. Further contributions to the Scheme will be assessed after considering the advice of the independent Scheme

Notes on the Accounts (continued)

5 Administrative expenses *(continued)*

b *Retirement benefits (continued)*

i *Pension schemes (continued)*

Actuary and taking into account long-term rates of returns on the underlying investments assessed with an appropriate degree of prudence.

The total pension cost for the year ended 31 December 2002 was £184 million (2001: £180 million), which includes £106 million (2001: £102 million) in respect of the Principal Scheme.

For CCF, retirement provision for employees in France is provided via both State and compulsory supplementary pension funds founded (via Government decree) on agreements between Employer Organisations and Unions. These 'compulsory supplementary' arrangements cover some 15,675 employees.

ii *FRS 17*

The financial assumptions used to calculate scheme liabilities for the group's main defined benefit pension schemes under FRS 17 are:

2002	*Discount rate*	*Inflation assumption*	*Rate of increase for pensions in payment and deferred pension*	*Rate of pay increase*
	%	%	%	%
United Kingdom	**5.6**	**2.25**	**2.25**	**2.75**
France	**5.5**	**2.0**	**2.0**	**3.5**
Switzerland	**3.75**	**1.5**	**0 - 1.5**	**2.5**

2001	*Discount rate*	*Inflation assumption*	*Rate of increase for pensions in payment and deferred pension*	*Rate of pay increase*
	%	%	%	%
United Kingdom	5.9	2.5	2.5	3.75
France	5.5	2.0	2.0	3.5
Switzerland	4.5	1.5	1.5	2.5

5 Administrative expenses *(continued)*

b *Retirement benefits (continued)*

ii *FRS 17(continued)*

The assets in the defined benefit schemes and the expected rates of return are:

	Expected rate of return at 31 December 2002	*Value at 31 December 2002*	*Expected rate of return at 31 December 2001*	*Value at 31 December 2001*
	%	**£m**	%	£m
Equities	**8.5**	**3,395**	7.5	3,941
Bonds	**4.9**	**1,293**	5.1	848
Property	**7.0**	**659**	7.5	655
Other	**3.65**	**263**	4.0	535
Total market value of assets		**5,610**		5,979
Present value of scheme liabilities		**(7,484)**		(6,816)
Deficit in the schemes*		**(1,874)**		(837)
Related deferred tax asset		**540**		209
Net pension liability		**(1,334)**		(628)
* Analysis of the deficit is as follows:				
The Principal Scheme		**(1,636)**		(661)
Other schemes — unfunded		**(199)**		(178)
Other schemes — funded		**(39)**		2
		(1,874)		(837)

The deficit in unfunded schemes has been fully provided (2001: £145 million).

The net pension liability will have a consequent effect on reserves when FRS 17 is fully implemented.

The Principal Scheme is closed to new entrants. For this scheme the current service cost will increase as the members of the scheme approach retirement under the projected unit credit method.

The following amounts would be reflected in the profit and loss account and statement of total consolidated recognised gains and losses on implementation of FRS 17:

	Year ended 31 December 2002
	£m
Amount that would be charged to operating profit	
Current service cost	**166**
Total operating charge	**166**
Amount that would be credited to other finance income	
Expected return on pension scheme assets	**405**
Interest on pension scheme liabilities	**(399)**
Net return	**6**
Amount that would be recognised in the statement of total consolidated recognised gains and losses	
Actual return less expected return on pension scheme assets	**(853)**
Experience gains and losses arising on the scheme liabilities	**(347)**
Changes in assumptions underlying the present value of the scheme liabilities	**251**
Actuarial loss	**(949)**

Notes on the Accounts (continued)

5 Administrative expenses (continued)

b *Retirement benefits (continued)*

ii *FRS 17(continued)*

	Year ended 31 December 2002 £m
Movement in pension schemes deficit during the year	
Deficit in the pension schemes at 1 January 2002	(837)
Movement in the year:	
Current service cost	(166)
Contributions	147
Other finance income	6
Actuarial loss	(949)
Acquisitions	(104)
Exchange and other movements	29
Deficit in the pension schemes at 31 December 2002	(1,874)
History of experience gains and losses	
Difference between expected and actual return on scheme assets:	
amount	(853)
percentage of scheme assets	(15%)
Experience gains and losses arising on scheme liabilities:	
Amount	(347)
percentage of the present value of scheme liabilities	(5%)
Total amount recognised in the statement of total consolidated recognised gains and losses:	
amount	(949)
percentage of the present value of scheme liabilities	(13%)

The Principal Scheme covers both UK employees of the group and UK employees of other HSBC Group companies. The deficit is the group's share of the Principal Scheme's deficit although the group's share increased following the acquisition of the business of HSBC Investment Bank plc.

iii *Post-retirement health-care benefits*

The group also provides post-retirement health-care benefits for certain pensioners and employees together with their dependent relatives. An actuarial assessment of the liabilities of the scheme, which is unfunded, is carried out on a regular basis by qualified actuaries. The liabilities are evaluated by discounting the expected future claims to a net present value.

The charge relating to post-retirement health-care is £12 million for the year (2001: £11 million).

The latest actuarial assessment was carried out at 31 December 2000 and updated to 31 December 2002. At 31 December 2002, the estimated present value of the post-retirement benefit obligation was £120 million (2001: £147 million) for the group and £120 million (2001: £140 million) for the bank, of which £105 million (2001: £98 million) has been provided for by the group and £105 million (2001: £92 million) has been provided for by the bank. Under FRS 17, the amount which would have been charged to operating profit as the current service charge is £nil. The total amount which would have been charged to other finance income as interest on scheme liabilities is £9 million. The amount which would have been credited to the statement of total consolidated recognised gains and losses due to changes in assumptions is £36 million. The main financial assumptions used to estimate the obligation at 31 December 2002 were price inflation of 2.5 per cent per annum (2001: 2.5 per cent), health-care claims cost escalation of 7.5 per cent per annum (2001: 7.5 per cent) and a discount rate of 5.6 per cent per annum (2001: 5.9 per cent). Under FRS 17, the deferred tax asset related to the unprovided liability of £15 million (2001: £49 million) would be £5 million (2001: £15 million).

5 Administrative expenses *(continued)*

c *Directors' emoluments*

The aggregate emoluments of the Directors of the bank, computed in accordance with Part I of Schedule 6 of the Act were:

	2002	2001
	£000	£000
Fees	**201**	215
Salaries and other emoluments	**1,487**	1,330
Discretionary bonuses	**982**	882
	2,670	2,427
Gains on exercise of share options	**229**	3,662

In addition, there are annual commitments under retirement benefit agreements with former Directors of £459,584 (2001: £471,811).

Retirement benefits accrue to three Directors under defined benefit schemes and to one Director under a money purchase scheme.

During the year, aggregate contributions to money purchase pension schemes were £529,000 (2001: £429,000).

Discretionary bonuses for Directors are based on a combination of individual and corporate performance and are determined by the Group Remuneration Committee of HSBC Holdings.

Details of individual Directors' remuneration are disclosed in the 'Directors' Remuneration Report' on page 52.

d *Auditors' remuneration*

Auditors' remuneration amounted to £5.6 million (2001: £4.9 million) including £1.5 million (2001: £1.4 million) which relates to the bank. £3.6 million (2001: £3.1 million) was paid to the bank's Auditors and their associates for non-audit work as analysed below:

	2002	2001
	£m	£m
Independent attestation		
Audit reports for US and other non-UK reporting	—	0.1
Reviews and reporting under regulatory requirements (including interim profits review)	**1.8**	1.5
	1.8	1.6
Financial advice		
Acquisition due diligence	**0.1**	0.2
Group reorganisations	**0.2**	0.3
Taxation services	**0.5**	0.4
Consultancy services	**0.6**	0.4
Other	**0.4**	0.2
	1.8	1.5
Total non-audit fees paid to Auditors	**3.6**	3.1

6 Profit on ordinary activities before tax

Profit on ordinary activities before tax is stated after:

		2002	2001
a	*Income*	**£m**	£m
	Aggregate rentals receivable, including capital repayments, under		
	— finance leases	**226**	252
	— hire purchase contracts	**552**	557
	— operating leases	**327**	323
	Increase in the value of long-term assurance business	**84**	140
	Profits less losses on debt securities and equities dealing	**(5)**	45
	Gain on disposal of investment securities	**104**	27

		2002	2001
b	*Charges on income*	**£m**	£m
	Charges incurred with respect to subordinated liabilities	**245**	316
	Finance charges in respect of finance leases and similar hire purchase contracts	**12**	12
	Rentals payable on premises held under operating leases	**149**	141
	Residential mortgage incentives	**18**	25

c *Gains on disposal of investments and tangible fixed assets*

Gains on disposal of investments and tangible fixed assets attracted a tax charge of £21 million (2001: £34 million).

7 Tax on profit on ordinary activities

The charge for taxation comprises:

	2002	2001*
	£m	£m
United Kingdom corporation tax charge	**540**	485
Adjustment in respect of prior periods	**(44)**	(115)
	496	370
Relief for overseas taxation	**(30)**	(13)
	466	357
Overseas taxation (including £(1) million (2001: £18 million) in respect of previous periods)	**234**	181
Joint ventures and associates	**3**	9
Current taxation	**703**	547
Origination and reversal of timing differences	**79**	59
Adjustment in respect of previous periods	**26**	116
Deferred taxation (Note 29a)	**105**	175
Total charge for taxation	**808**	722

* *Figures for 2001 have been restated to reflect the adoption of Financial Reporting Standard 19, 'Deferred Tax', details of which are set out in Note1(d) on the Accounts on page 64.*

During the year, the group provided for UK corporation tax at 30 per cent (2001: 30 per cent).

The tax charge includes £18 million (2001: £31 million) in respect of the tax attributable to the increase in the value of long-term assurance business attributable to shareholders.

7 Tax on profit on ordinary activities *(continued)*

Analysis of overall tax charge	**2002**	2001 *
	£m	£m
Taxation at UK corporation tax rate of 30% (2001: 30%)	**685**	687
Other non-deductible items including unrelieved losses	**12**	6
Tax-free gains	**(5)**	(38)
Impact of differently taxed overseas profits in principal locations	**(36)**	(50)
Amortisation of goodwill	**141**	140
Prior year adjustments	**(22)**	(2)
Other items	**33**	(21)
Timing differences impact on current tax	**(105)**	(175)
Current tax charge	**703**	547
Deferred tax charge	**105**	175
Overall tax charge	**808**	722

* *Figures for 2001 have been restated to reflect the adoption of Financial Reporting Standard 19, 'Deferred Tax', details of which are set out in Note1(d) on the Accounts on page 64.*

8 Profit of the bank

The profit of the bank for the year attributable to shareholders was £1,854 million (2001: £1,712 million, after restating for FRS 19, details of which are set out in Note 1(d) on the Accounts on page 64).

9 Dividends

	2002	2001
	£m	£m
Equity		
Ordinary dividends		
— paid	**600**	600
— proposed	**500**	900
	1,100	1,500
Non-equity		
Preference dividends	**44**	63
	1,144	1,563

Non-cumulative dividends of US$1.344 and US$0.546 per share per annum were paid on the Series 1 and Series 2 US$ Second preference shares respectively, pro rata to the date of redemption on 7 March 2002.

During the year a further 2,000,000 Third preference shares were issued. Dividends are payable annually at a rate of 7.5 per cent per annum.

10 Earnings per ordinary share

Basic and diluted earnings per ordinary share are calculated by dividing the profit for the financial year attributable to equity shareholders, after deducting preference dividends, of £1,335 million (2001: £1,407 million, after restating for FRS 19, details of which are set out in Note 1(d) on the Accounts on page 64) by the weighted average number of ordinary shares in issue in 2002 of 797 million (2001: 797 million).

Notes on the Accounts (continued)

11 Treasury bills and other eligible bills

	group				*bank*			
	Book value	*Market valuation*	*Book value*	*Market valuation*	*Book value*	*Market valuation*	*Book value*	*Market valuation*
	2002	**2002**	2001	2001	**2002**	**2002**	2001	2001
	£m	**£m**	£m	£m	**£m**	**£m**	£m	£m
Investment securities								
— treasury bills and similar securities	**948**	**952**	2,579	2,586	**367**	**367**	2,136	2,141
— other eligible bills	**630**	**630**	343	343	**630**	**630**	343	343
	1,578	**1,582**	2,922	2,929	**997**	**997**	2,479	2,484
Other securities								
— treasury bills and similar securities	**469**		13		**433**		13	
— other eligible bills	**—**		2		**—**		—	
	469		15		**433**		13	
	2,047		2,937		**1,430**		2,492	

Investment securities:	*Cost and book value*
group	**£m**
At 1 January 2002	**2,922**
Additions	**7,037**
Disposals and amounts repaid	**(8,416)**
Amortisation of discounts and premiums	**55**
Exchange and other movements	**(20)**
At 31 December 2002	**1,578**
bank	**£m**
At 1 January 2002	**2,479**
Additions	**6,110**
Disposals and amounts repaid	**(7,653)**
Amortisation of discounts and premiums	**46**
Exchange and other movements	**15**
At 31 December 2002	**997**

11 Treasury bills and other eligible bills *(continued)*

The maturities of investment treasury bills and other eligible bills at 31 December 2002 are analysed as follows:

	group		*bank*	
	Book value	*Market valuation*	*Book value*	*Market valuation*
	£m	**£m**	**£m**	**£m**
1 year or less	**1,384**	**1,386**	**994**	**994**
Greater than 1 year	**194**	**196**	**3**	**3**
	1,578	**1,582**	**997**	**997**

The net unamortised discounts on investment securities were:

	group	*bank*
	2002	**2002**
	£m	**£m**
	7	**5**

12 Credit risk management

The group's credit risk management process is discussed in the 'Financial Review' section in the paragraph headed 'Credit Risk Management' on page 34.

13 Loans and advances to banks

	group		*bank*	
	2002	2001	**2002**	2001
	£m	£m	**£m**	£m
Remaining maturity				
— repayable on demand	**7,259**	6,153	**5,252**	4,427
— 3 months or less but not repayable on demand	**15,716**	20,219	**7,049**	7,758
— 1 year or less but over 3 months	**2,854**	4,747	**1,040**	1,612
— 5 years or less but over 1 year	**548**	934	**471**	298
— over 5 years	**264**	293	**415**	488
Specific provisions for bad and doubtful debts (Note 15)	**(14)**	(15)	**(3)**	(3)
	26,627	32,331	**14,224**	14,580
Amounts include:				
Subordinated	**45**	66	**—**	—
Due from subsidiary undertakings				
— unsubordinated			**1,051**	1,085
Due from fellow subsidiary undertakings				
— unsubordinated	**1,067**	4,106	**866**	3,050

Notes on the Accounts (continued)

14 Loans and advances to customers

	group		bank	
	2002	2001	**2002**	2001
	£m	£m	**£m**	£m
Remaining maturity				
— repayable on demand or at short notice	**18,413**	15,119	**12,954**	10,923
— 3 months or less but not repayable on demand or at short notice	**19,714**	18,364	**12,688**	11,502
— 1 year or less but over 3 months	**12,308**	10,121	**7,954**	6,718
— 5 years or less but over 1 year	**26,363**	22,897	**20,094**	18,167
— over 5 years	**30,361**	24,533	**23,839**	19,429
General and specific provisions for bad and doubtful debts (Note 15)	**(2,252)**	(2,033)	**(1,322)**	(1,167)
	104,907	89,001	**76,207**	65,572
Amounts include:				
Subordinated	**114**	76	**15**	—
Due from subsidiary undertakings — unsubordinated			**6,043**	5,256
Due from fellow subsidiary undertakings — unsubordinated	**440**	1,252	**439**	1,156
Due from joint ventures — unsubordinated	**203**	607	**165**	139

Securitisation transactions

Loans and advances to customers include balances that have been securitised. Certain of these balances meet the requirements for linked presentation under FRS 5, 'Reporting the substance of transactions'.

The non-recourse finance has been netted against customer loans as follows:

	2002	2001
	£m	£m
Customer loans	**1,423**	1,287
Non-recourse finance	**(1,271)**	(1,145)
Funding provided by the bank	**152**	142

14 Loans and advances to customers *(continued)*

The bank has securitised a designated portion of its corporate loan portfolio. The transaction was effected through a declaration of trust in favour of Clover Securitisation Limited. Clover Securitisation Limited holds its beneficial interest in the trust for Clover Funding No. 1 plc, Clover Funding No. 2 plc, Clover Funding No. 3 plc, Clover Funding No. 4 plc (collectively 'Clover Funding') and the bank.

To fund the acquisition of this beneficial interest, Clover Funding has issued £1,423 million (2001: £1,287 million) floating rate notes ('FRNs'). The offering circulars for the FRNs state that they are the obligations of Clover Funding only and are not guaranteed by, or the responsibility of, any other party. Non-returnable proceeds of £1,271 million (2001: £1,145 million) received by the bank from Clover Funding have been deducted from 'Loans and advances to customers'. Clover Securitisation Limited has entered into swap agreements with the bank under which Clover Securitisation Limited pays the floating rate of interest on the loans and receives interest linked to three-month London Interbank Offered Rate ('LIBOR'). The proceeds generated from the loans are used in priority to meet the claims of the FRN holders, and amounts payable in respect of the interest rate swap arrangements after the payment of trustee and administration expenses.

There is no provision whatsoever, either in the financing arrangements or otherwise, whereby the bank or any part of the group has a right or obligation either to keep the loans and advances on repayment of the finance or to repurchase them at any time other than in certain circumstances where the bank is in breach of warranty.

The bank is not obliged to support any losses that may be suffered by the FRN holders and does not intend to provide such support.

The bank has taken up £41 million (2001: £35 million) of subordinated FRNs that are repayable after payments in respect of senior FRNs. The bank has made subordinated loans of £26 million (2001: £23 million) to Clover Funding that are repayable after all other payments. Interest is payable on the subordinated FRNs and subordinated loans conditional upon Clover Funding having funds available.

Clover Securitisation Limited's entire share capital is held by Clover Holdings Limited. Clover Funding's entire share capital is held by Clover Holdings Limited. Clover Holdings Limited's entire share capital is held by trustees under the terms of a trust for charitable purposes.

The bank recognised net income of £3 million (2001: £2 million) which comprised £64 million (2001: £31 million) interest receivable by Clover Funding and £61 million (2001: £29 million) of interest on FRNs and other third-party expenses payable by Clover Funding.

Notes on the Accounts (continued)

15 Provisions for bad and doubtful debts

a *Movements on provisions for bad and doubtful debts*

	Specific	*General*	*Total*	*Specific*	*General*	*Total*
	2002	**2002**	**2002**	2001	2001	2001
	£m	**£m**	**£m**	£m	£m	£m
group						
At 1 January	**1,502**	**546**	**2,048**	1,431	528	1,959
Amounts written off	**(290)**	**—**	**(290)**	(303)	—	(303)
Recoveries of amounts written off in previous years	**41**	**—**	**41**	41	—	41
Charge/(release) to the profit and loss account	**412**	**(35)**	**377**	322	(14)	308
Acquisitions	**37**	**15**	**52**	97	19	116
Disposal of subsidiary undertakings	**—**	**—**	**—**	(17)	—	(17)
Exchange and other movements	**37**	**1**	**38**	(69)	13	(56)
At 31 December	**1,739**	**527**	**2,266**	1,502	546	2,048
bank						
At 1 January	**804**	**366**	**1,170**	748	361	1,109
Amounts written off	**(210)**	**—**	**(210)**	(228)	—	(228)
Recoveries of amounts written off in previous years	**33**	**—**	**33**	37	—	37
Charge/(release) to the profit and loss account	**369**	**(32)**	**337**	249	2	251
Exchange and other movements	**(5)**	**—**	**(5)**	(2)	3	1
At 31 December	**991**	**334**	**1,325**	804	366	1,170

	group		*bank*	
	2002	2001	**2002**	2001
	£m	£m	**£m**	£m
Included in:				
Loans and advances to banks (Note 13)	**14**	15	**3**	3
Loans and advances to customers (Note 14)	**2,252**	2,033	**1,322**	1,167
	2,266	2,048	**1,325**	1,170

15 Provisions for bad and doubtful debts *(continued)*

b *Movements on suspended interest account*

	group		*bank*	
	2002	2001	**2002**	2001
	£m	£m	**£m**	£m
At 1 January	**80**	69	**31**	29
Amounts written off	**(12)**	(11)	**(8)**	(7)
Interest suspended during the year	**44**	45	**22**	17
Suspended interest recovered	**(23)**	(19)	**(7)**	(8)
Exchange and other movements	**(9)**	(4)	**(3)**	—
At 31 December	**80**	80	**35**	31

c *Non-performing loans*

	group		*bank*	
	2002	2001	**2002**	2001
	£m	£m	**£m**	£m
Loans on which interest has been suspended (net of suspended interest)	**1,321**	1,098	**909**	801
Provisions	**(626)**	(478)	**(364)**	(324)
	695	620	**545**	477
Other non-performing loans	**1,502**	1,409	**887**	721
Provisions	**(1,113)**	(1,024)	**(627)**	(480)
	389	385	**260**	241
Total non-performing loans (net of provisions)	**1,084**	1,005	**805**	718

16 Concentrations of exposure

The group has the following concentrations of loans and advances to customers:

	2002	2001
	£m	£m
Total gross advances to customers:		
Residential mortgages	**24,061**	18,613
Other personal	**18,354**	14,893
Commercial, industrial and international trade	**27,622**	25,643
Commercial real estate	**7,377**	5,917
Other property related	**2,464**	2,388
Government	**1,382**	1,221
Non-bank financial institutions	**9,869**	8,858
Other commercial	**16,109**	13,570
	107,238	91,103

The analysis of concentration of exposure is based on the categories used by the group to manage the associated risks. Of total loans and advances to customers gross of provisions, £75,299 million (2001: £63,017 million) was advanced by operations located in the United Kingdom.

Other commercial includes advances in respect of transport, energy and agriculture.

Notes on the Accounts (continued)

17 Debt securities

	group				bank			
	Book value	*Market valuation*	*Book value*	*Market valuation*	*Book value*	*Market valuation*	*Book value*	*Market valuation*
	2002	**2002**	2001	2001	**2002**	**2002**	2001	2001
Issued by public bodies	**£m**	**£m**	£m	£m	**£m**	**£m**	£m	£m
Investment securities								
— government securities and US government agencies	**6,077**	**6,215**	7,961	8,017	**1,564**	**1,570**	3,187	3,198
— other public sector securities	**806**	**870**	1,081	1,098	**61**	**62**	70	71
	6,883	**7,085**	9,042	9,115	**1,625**	**1,632**	3,257	3,269
Other debt securities								
— government securities and US government agencies	**8,898**		5,398		**2,229**		1,815	
— other public sector securities	**67**		5		**41**		4	
	8,965		5,403		**2,270**		1,819	
Issued by other bodies								
Investment securities								
— bank and building society certificates of deposit	**240**	**240**	961	961	**101**	**101**	484	484
— other securities	**13,448**	**13,728**	9,191	9,252	**3,173**	**3,237**	2,795	2,823
	13,688	**13,968**	10,152	10,213	**3,274**	**3,338**	3,279	3,307
Other debt securities								
— bank and building society certificates of deposit	**5,890**		7,024		**5,660**		6,070	
— other securities	**9,522**		10,256		**7,760**		7,944	
	15,412		17,280		**13,420**		14,014	
	44,948		41,877		**20,589**		22,369	
Due within 1 year	**15,532**		15,011		**10,310**		10,615	
Due 1 year and over	**29,416**		26,866		**10,279**		11,754	
	44,948		41,877		**20,589**		22,369	
Amounts include:								
Subordinated debt securities	**153**		115		**104**		94	
Unamortised net premiums/(discounts) on investment securities	**167**		(23)		**171**		73	
Investment securities								
— listed	**17,097**	**17,542**	14,727	14,864	**3,706**	**3,769**	3,841	3,874
— unlisted	**3,474**	**3,511**	4,467	4,464	**1,193**	**1,201**	2,695	2,702
	20,571	**21,053**	19,194	19,328	**4,899**	**4,970**	6,536	6,576
Other debt securities								
— listed	**13,698**		11,457		**8,324**		7,253	
— unlisted	**10,679**		11,226		**7,366**		8,580	
	24,377		22,683		**15,690**		15,833	
	44,948		41,877		**20,589**		22,369	

17 Debt securities *(continued)*

Where securities are carried at market valuation, and the market valuation is higher than cost, the difference between cost and market valuation is not disclosed as it cannot be determined without unreasonable expense.

The above market valuations do not take account of transactions entered into to hedge the value of the group's investment securities. If these transactions were included, the market valuation of investment securities would be £20,782 million for the group (2001: £19,269 million) and £4,970 million (2001: £6,576 million) for the bank.

Investment securities:

	Cost	*Provisions*	*Book value*
	£m	**£m**	**£m**
group			
At 1 January 2002	**19,215**	**(21)**	**19,194**
Acquisitions	**1,367**	**—**	**1,367**
Additions	**12,697**	**(2)**	**12,695**
Disposals and amounts repaid	**(11,495)**	**(9)**	**(11,504)**
Amortisation of discounts and premiums	**(154)**	**—**	**(154)**
Exchange and other movements	**(1,032)**	**5**	**(1,027)**
At 31 December 2002	**20,598**	**(27)**	**20,571**
bank			
At 1 January 2002	**6,540**	**(4)**	**6,536**
Acquisitions	**59**	**—**	**59**
Additions	**3,592**	**(2)**	**3,590**
Disposals and amounts repaid	**(5,050)**	**(1)**	**(5,051)**
Amortisation of discounts and premiums	**(161)**	**—**	**(161)**
Exchange and other movements	**(75)**	**1**	**(74)**
At 31 December 2002	**4,905**	**(6)**	**4,899**

18 Equity shares

	group				*bank*			
	Book value	*Market valuation*	*Book value*	*Market valuation*	*Book value*	*Market valuation*	*Book value*	*Market valuation*
	2002	**2002**	2001	2001	**2002**	**2002**	2001	2001
	£m	**£m**	£m	£m	**£m**	**£m**	£m	£m
Investment securities								
— listed	**435**	**477**	553	566	**27**	**40**	40	45
— unlisted	**1,131**	**1,286**	911	983	**86**	**109**	108	118
	1,566	**1,763**	1,464	1,549	**113**	**149**	148	163
Other securities								
— listed	**1,843**		753		**1,095**		84	
— unlisted	**74**		70		**1**		1	
	1,917		823		**1,096**		85	
	3,483		2,287		**1,209**		233	

Where securities are carried at market valuation, and the market valuation is higher than cost, the difference between cost and market valuation is not disclosed as it cannot be determined without unreasonable expense.

Notes on the Accounts (continued)

18 Equity shares *(continued)*

Investment securities:

	Cost	*Provisions*	*Book value*
	£m	**£m**	**£m**
group			
At 1 January 2002	**1,616**	**(152)**	**1,464**
Acquisitions	**330**	**(44)**	**286**
Additions	**814**	**—**	**814**
Disposals	**(976)**	**39**	**(937)**
Provisions made	**—**	**(98)**	**(98)**
Exchange and other movements	**63**	**(26)**	**37**
At 31 December 2002	**1,847**	**(281)**	**1,566**
bank			
At 1 January 2002	**153**	**(5)**	**148**
Acquisitions	**114**	**(27)**	**87**
Additions	**9**	**—**	**9**
Disposals	**(139)**	**2**	**(137)**
Provisions made	**—**	**(6)**	**(6)**
Exchange and other movements	**25**	**(13)**	**12**
At 31 December 2002	**162**	**(49)**	**113**

Included in investment securities is £2 million, after amortisation, of HSBC Holdings' shares (2001: £1 million) held in trust for the purposes of conditional awards under the Restricted Share Plan, details of which are provided in the 'Directors' Remuneration Report' on page 56. At 31 December 2002, the trust held 974,815 ordinary shares (2001: 642,983) of nominal value US$0.50 each with a market value at that date of £7 million (2001: £5 million) in respect of these conditional awards.

Also included within investment securities is £13 million of HSBC Holdings' shares (2001: £7 million) held in trust which may be used in respect of the exercise of share options. At 31 December 2002, the trust held 1,482,249 ordinary shares (2001: 796,700) of US$0.50 each with a market value of £10 million (2001: £6 million) in respect of these option holders.

19 Interests in joint ventures

a *Movements in interests in joint ventures*

	group
	£m
At 1 January 2002	**164**
Disposals	**(74)**
Retained profits and losses	**3**
Amortisation of goodwill	**(6)**
Exchange and other movements	**2**
At 31 December 2002	**89**

None of the joint ventures is listed or is a bank.

19 Interests in joint ventures *(continued)*

b *Principal joint venture as at 31 December 2002*

	Country of incorporation	*Principal activity*	*Interest in equity capital*
Framlington Group Limited	UK	Asset management	51%

During the year, the group sold its 49 per cent interest in Lixxbail.

Framlington Group Limited prepares its financial statements up to 31 December and its principal country of operation is the United Kingdom.

The group's share of total operating income in joint ventures is £27 million (2001: £48 million).

The group's share of contingent liabilities in joint ventures is £nil (2001: £39 million).

c *Goodwill*

Included within the group's share of gross assets of joint ventures is goodwill, as follows:

	group
	£m
Cost	
At 1 January 2002	**136**
Disposals	**(43)**
Exchange and other movements	**1**
At 31 December 2002	**94**

	group
	£m
Accumulated amortisation	
At 1 January 2002	**9**
Disposals	**(4)**
Charge to the profit and loss account	**6**
At 31 December 2002	**11**
Net book value at 31 December 2002	**83**

The goodwill is being amortised over 20 years, reflecting its expected useful life.

Notes on the Accounts (continued)

20 Interests in associates

a *Movements in interests in associates*

	group	*bank*
	£m	**£m**
At 1 January 2002	**128**	**7**
Acquisitions	**5**	**—**
Additions	**4**	**—**
Disposals	**(18)**	**—**
Retained losses	**(12)**	**(1)**
Exchange and other movements	**2**	**(1)**
At 31 December 2002	**109**	**5**

	group		*bank*	
	2002	2001	**2002**	2001
	£m	£m	**£m**	£m
Shares in banks	**7**	20	**—**	—
Other	**102**	108	**5**	7
	109	128	**5**	7

None of the associates is listed.

On the historical cost basis, the bank's interests in associates would have been included as follows:

	2002	2001
	£m	£m
Cost	**15**	15
Provisions	**(10)**	(9)
	5	6

b *Principal associate as at 31 December 2002*

	Country of incorporation	*Principal activity*	*Interest in equity capital*
Erisa	France	Insurance	49.99%

21 Investments in subsidiary undertakings

a *Movements in investments in subsidiary undertakings*

	£m
At 1 January 2002*	**13,688**
Additions	**916**
Redemption of shares	**(164)**
Write-down to net asset value including attributable goodwill	**(71)**
Exchange and other movements	**3**
At 31 December 2002	**14,372**

* *Figures for 2001 have been restated to reflect the adoption of Financial Reporting Standard 19, 'Deferred Tax', details of which are set out in Note1(d) on the Accounts on page 64.*

The above amount represents the direct interests of the bank in its subsidiary undertakings. Interests in subsidiary undertakings include £7,892 million (2001: £7,984 million) representing interests in banks.

On the historical cost basis, the bank's interests in subsidiary undertakings would have been included as follows:

	2002 **£m**	2001 £m
Cost	**13,763**	13,043
Provisions	**(1)**	(36)
	13,762	13,007

b *Principal subsidiary undertakings as at 31 December 2002*

	Country of incorporation
CCF S.A. (formerly Crédit Commercial de France S.A.) (99.99% owned)	France
HSBC Asset Finance (UK) Limited	England
HSBC Bank A.S.	Turkey
HSBC Bank International Limited	Jersey
HSBC Bank Malta p.l.c. (70.03% owned)	Malta
HSBC Guyerzeller Bank AG (83.99% owned)	Switzerland
HSBC Invoice Finance (UK) Limited	England
HSBC Life (UK) Limited	England
HSBC Rail (UK) Limited	England
HSBC Republic Bank (Guernsey) Limited (97.82% owned)	Guernsey
HSBC Republic Bank (Suisse) SA (97.82% owned)	Switzerland
HSBC Republic Bank (UK) Limited (97.82% owned)	England
HSBC Trinkaus & Burkhardt KGaA (73.47% owned)	Germany
HSBC Trust Company (UK) Limited	England

Details of all subsidiary undertakings will be annexed to the next annual return of the bank. All of the above subsidiary undertakings are engaged in the business of banking or other financial services.

Notes on the Accounts (continued)

21 Investments in subsidiary undertakings *(continued)*

b *Principal subsidiary undertakings as at 31 December 2002 (continued)*

Except where indicated otherwise, the issued equity capital of the above undertakings is wholly owned by the group and is held by subsidiaries of the bank except for the following entities:

CCF S.A.
HSBC Asset Finance (UK) Limited
HSBC Bank A.S.
HSBC Life (UK) Limited
HSBC Trust Company (UK) Limited

c *Acquisitions*

On 1 April 2002, the group acquired 97.82 per cent of the issued share capital of HSBC Republic Holdings (C.I.) Limited from HSBC Investment Bank Holdings BV for a cash consideration of £97 million. Goodwill of £52 million arose on the acquisition.

On 1 April 2002, the group acquired 97.82 per cent of the issued share capital of HSBC International Trustee Limited from HSBC Investment Bank Holdings BV for a cash consideration of £116 million. Goodwill of £113 million arose on the acquisition.

On 1 April 2002, the group acquired 97.45 per cent of the issued share capital of HSBC Republic Bank (Cyprus) Limited from HSBC Investment Bank Holdings BV for a cash consideration of £8 million.

On 1 July 2002, the group acquired 100 per cent of the issued share capital of HSBC Germany Holdings GmbH from HSBC Investment Bank Holdings BV for a cash consideration of £356 million. HSBC Germany Holdings GmbH holds 73.47 per cent of the issued share capital of HSBC Trinkaus & Burkhardt KGaA.

On 1 July 2002, the group acquired 97.82 per cent of the issued share capital of HSBC Republic Bank (UK) Limited from HSBC Investment Bank plc for a cash consideration of £256 million. Goodwill of £125 million arose on the acquisition and includes £17 million of goodwill in respect of Property Vision.

On 1 July 2002, the bank acquired 100 per cent of the issued share capital of HSBC Select (UK) Limited from HSBC Insurance Brokers Limited for nil consideration. Goodwill of £3 million arose on the acquisition.

On 1 July 2002, the group acquired the business in respect of 11 branches of Banque Worms from Deutsche Bank Group for a cash consideration of £6 million. Goodwill of £6 million arose on the acquisition.

On 1 September 2002, the group acquired 60 per cent of the issued share capital of Equator Holdings Limited from HSBC Investment Bank plc for a cash consideration of £9 million.

On 19 September 2002, the group acquired 100 per cent of the issued share capital of Benkar Tuketici Finansmani ve Kart Hizmetleri A.S. for a consideration of £47 million. Of this, £20 million is deferred consideration, payable over five years and conditional on achievement of specific business objectives. Goodwill of £35 million arose on the acquisition. The fair values of the assets and liabilities acquired have been determined only on a provisional basis pending completion of the fair value appraisal process.

On 1 November 2002, the bank acquired 100 per cent of the issued share capital of Merrill Lynch HSBC Limited from Merrill Lynch HSBC Holdings Limited for nil consideration. A discount of £58 million arose on the acquisition.

On 30 November 2002, the group acquired the business of HSBC Investment Bank plc for £87 million from HSBC Investment Bank Holdings plc.

Cash consideration of £3 million and goodwill of £2 million arose on other acquisitions in the year.

An increase in stake in an existing subsidiary is excluded from the table on the following page. On 31 October 2002, the group increased its stake in Banque du Louvre from 88.86 per cent to 100 per cent for a cash consideration of £17 million. Goodwill of £7 million arose on the acquisition.

All acquisitions have been accounted for on an acquisitions basis.

21 Investments in subsidiary undertakings *(continued)*

c *Acquisitions (continued)*

The assets and liabilities at the dates of acquisition and the total consideration paid are set out in the following table:

	Fair value
	£m
At the date of acquisition:	
Cash and balances at central banks	**34**
Loans and advances to banks	**7,105**
Loans and advances to customers	**6,274**
Debt securities	**2,050**
Equity shares	**1,751**
Interests in associates	**5**
Tangible fixed assets	**136**
Other asset categories	**2,489**
Deposits by banks	**(6,017)**
Customer accounts	**(9,173)**
Debt securities in issue	**(437)**
Subordinated capital	
— dated loan capital	**(160)**
Provision for liabilities and charges	**(178)**
Other liability categories	**(3,064)**
Total	**815**
Less: minority interests	**(108)**
Net assets acquired	**707**
Goodwill attributable	**278**
Total consideration	**985**

There were no material differences between book value and fair value.

Notes on the Accounts (continued)

22 Intangible fixed assets

Goodwill	*group*	*bank*
	2002	**2002**
	£m	**£m**
Cost		
At 1 January 2002*	**8,980**	**45**
Additions (positive goodwill of £343 million, negative goodwill of £58 million)	**285**	**1**
Disposal of subsidiary undertaking	**(34)**	**—**
Exchange and other movements	**181**	**—**
At 31 December 2002	**9,412**	**46**
Accumulated amortisation		
At 1 January 2002	**577**	**5**
Charge to the profit and loss account (net of negative goodwill of £7 million)	**482**	**3**
Disposal of subsidiary undertaking	**(3)**	**—**
Exchange and other movements	**18**	**—**
At 31 December 2002	**1,074**	**8**
Net book value at 31 December 2002 (net of negative goodwill of £51 million)	**8,338**	**38**
Net book value at 31 December 2001*	8,403	40

** Figures for 2001 have been restated to reflect the adoption of Financial Reporting Standard 19, 'Deferred Tax', details of which are set out in Note 1(d) on the Accounts on page 64.*

Additions represent goodwill arising on the acquisition of and increased holdings in subsidiaries and businesses during 2002.

Positive goodwill on the acquisition of CCF S.A. and HSBC Private Banking Holdings (Suisse) SA and their subsidiaries is being amortised over 20 years. Other positive goodwill is being amortised over periods of up to 15 years. Negative goodwill is being credited to the profit and loss account over five years, the period to be benefited.

23 Tangible fixed assets

a *Movements on tangible fixed assets*

group	*Freehold land and buildings*	*Long leasehold land and buildings*	*Short leasehold land and buildings*	*Equipment, fixtures and fittings*	*Equipment on operating leases*	*Total*
	£m	**£m**	**£m**	**£m**	**£m**	**£m**
Cost or valuation						
At 1 January 2002	**1,120**	**594**	**326**	**2,007**	**2,403**	**6,450**
Additions	**17**	**87**	**8**	**346**	**425**	**883**
Disposals	**(61)**	**—**	**(10)**	**(167)**	**(227)**	**(465)**
Acquisitions	**84**	**3**	**3**	**45**	**1**	**136**
Deficit on revaluation taken to profit and loss	**(21)**	**—**	**—**	**—**	**—**	**(21)**
Transfer of accumulated depreciation arising on revaluation	**(39)**	**(1)**	**—**	**—**	**—**	**(40)**
Deficit on revaluation	**(1)**	**(44)**	**—**	**—**	**—**	**(45)**
Exchange and other movements	**68**	**(1)**	**(49)**	**83**	**(7)**	**94**
At 31 December 2002	**1,167**	**638**	**278**	**2,314**	**2,595**	**6,992**
Accumulated depreciation						
At 1 January 2002	**(32)**	**(3)**	**(174)**	**(1,251)**	**(566)**	**(2,026)**
Disposals	**4**	**—**	**7**	**129**	**152**	**292**
Transfer of accumulated depreciation arising on revaluation	**39**	**1**	**—**	**—**	**—**	**40**
Charge to the profit and loss account	**(24)**	**(2)**	**(9)**	**(242)**	**(157)**	**(434)**
Exchange and other movements	**(19)**	**2**	**2**	**(61)**	**2**	**(74)**
At 31 December 2002	**(32)**	**(2)**	**(174)**	**(1,425)**	**(569)**	**(2,202)**
Net book value						
At 31 December 2002	**1,135**	**636**	**104**	**889**	**2,026**	**4,790**
At 31 December 2001	1,088	591	152	756	1,837	4,424

Notes on the Accounts (continued)

23 Tangible fixed assets *(continued)*

a *Movements on tangible fixed assets (continued)*

	Freehold land and buildings	*Long leasehold land and buildings*	*Short leasehold land and buildings*	*Equipment, fixtures and fittings*	*Total*
bank	**£m**	**£m**	**£m**	**£m**	**£m**
Cost or valuation					
At 1 January 2002	**446**	**581**	**202**	**1,226**	**2,455**
Additions	**5**	**87**	**7**	**239**	**338**
Disposals	**—**	**—**	**(9)**	**(52)**	**(61)**
Acquisitions	**—**	**3**	**2**	**16**	**21**
Deficit on revaluation taken to profit and loss	**(2)**	**—**	**—**	**—**	**(2)**
Transfer of accumulated depreciation arising on revaluation	**(9)**	**(1)**	**—**	**—**	**(10)**
Deficit on revaluation	**13**	**(44)**	**—**	**—**	**(31)**
Exchange and other movements	**(6)**	**(1)**	**(1)**	**(1)**	**(9)**
At 31 December 2002	**447**	**625**	**201**	**1,428**	**2,701**
Accumulated depreciation					
At 1 January 2002	**(23)**	**(3)**	**(135)**	**(734)**	**(895)**
Disposals	**—**	**—**	**7**	**47**	**54**
Transfer of accumulated depreciation arising on revaluation	**9**	**1**	**—**	**—**	**10**
Charge to the profit and loss account	**(14)**	**(1)**	**(8)**	**(149)**	**(172)**
Exchange and other movements	**5**	**—**	**1**	**—**	**6**
At 31 December 2002	**(23)**	**(3)**	**(135)**	**(836)**	**(997)**
Net book value					
At 31 December 2002	**424**	**622**	**66**	**592**	**1,704**
At 31 December 2001	423	578	67	492	1,560

b *Assets held under finance leases*

The net book amount of equipment, fixtures and fittings included assets held under finance leases of £5 million (2001: £22 million) for the group and £nil million (2001: £3 million) for the bank, on which the depreciation charge was £2 million (2001: £5 million) for the group and £2 million (2001: £7 million) for the bank. The net book amount of equipment on operating leases included assets held under finance leases of £117 million (2001: £120 million) for the group on which the depreciation charge was £3 million (2001: £2 million).

23 Tangible fixed assets *(continued)*

c *Valuations*

	group		*bank*	
	2002	2001	**2002**	2001
	£m	£m	**£m**	£m
Cost or valuation of freehold and long leasehold land and buildings:				
At valuation	**1,787**	1,170	**1,062**	485
At cost	**18**	544	**10**	542
	1,805	1,714	**1,072**	1,027
On the historical cost basis, freehold and long leasehold land and buildings would have been included as follows:				
Cost	**1,900**	1,670	**1,087**	993
Accumulated depreciation	**(267)**	(284)	**(119)**	(147)
Net book value	**1,633**	1,386	**968**	846

The group values its freehold and long leasehold properties on an annual basis. In September 2002, the group's freehold and long leasehold properties were revalued on an existing use basis or open market value as appropriate or, in the case of a few specialised properties, at depreciated replacement cost. The properties were revalued either by professional external valuers or by professionally qualified staff. The valuation has been updated for any material changes at 31 December 2002.

As a result of the revaluation, there was a deficit below the net book value of land and buildings of £66 million (bank: £33 million), of which £44 million, net of minority interests of £1 million and deficits taken to the profit and loss account of £21 million, (bank: £31 million, net of deficits taken to the profit and loss account of £2 million) has been included in the revaluation reserve at 31 December 2002.

d *Land and buildings occupied for own activities*

	group		*bank*	
	2002	2001	**2002**	2001
	£m	£m	**£m**	£m
Net book value	**1,642**	1,233	**936**	510

Land and buildings with a net book value of £22 million (2001: £39 million) are occupied by HSBC Holdings plc and its subsidiaries other than the group.

23 Tangible fixed assets *(continued)*

e *Residual values of equipment on operating leases*

Included in the net book value of equipment on operating leases are residual values at the end of current lease terms, which will be recovered through re-letting or disposal in the following periods:

	2002	2001
	£m	£m
Within 1 year	**347**	171
Between 1 and 2 years	**687**	267
Between 2 and 5 years	**180**	702
Over 5 years	**443**	363
	1,657	1,503

Residual value risk arises in relation to an operating lease transaction to the extent that the actual value of the leased asset at the end of the lease term (the residual value), recovered through disposing of or re-letting the asset at the end of the lease term, could be different to that projected at the inception of the lease. Residual value exposure is regularly monitored by the business through reviewing the recoverability of the residual value projected at lease inception. This entails considering the ability to re-let and projected disposal proceeds of operating lease assets at the end of their lease terms. Provision is made to the extent that the carrying values of leased assets are impaired through residual values not being fully recoverable.

24 Other assets

	group		*bank*	
	2002	2001*	**2002**	2001
	£m	£m	**£m**	£m
Bullion	**5**	2	**1**	2
Assets, including gains, resulting from off-balance-sheet interest rate, exchange rate and equities contracts that are marked to market	**9,530**	6,890	**6,699**	5,882
Deferred taxation (Note 29a)	**55**	57	**167**	87
Long-term assurance assets attributable to policyholders (Note 28)	**3,263**	3,420	**—**	—
Other	**3,761**	4,094	**849**	1,730
	16,614	14,463	**7,716**	7,701
Assets, including gains, resulting from off-balance-sheet interest rate, exchange rate and equities contracts that are marked to market, include unsubordinated amounts:				
Due from subsidiary undertakings			**738**	215
Due from fellow subsidiary undertakings	**1,212**	1,030	**1,142**	977

* *Figures for 2001 have been restated to reflect the adoption of Financial Reporting Standard 19, 'Deferred Tax', details of which are set out in Note 1(d) on the Accounts on page 64.*

24 Other assets *(continued)*

'Other' includes the surplus retained in long-term assurance funds and the net present value of policies in force. These assets form part of the total value of the group's interest in long-term assurance business as follows:

	2002	2001
	£m	£m
Net tangible assets of long-term assurance subsidiaries	**41**	26
Surplus retained in long-term assurance funds and net present value of policies in force	**559**	488
Total long-term assurance business attributable to shareholders	**600**	514

The increase in the value of long-term assurance business attributable to shareholders which is included in the consolidated profit and loss account amounts to £84 million (2001: £140 million) before tax and £66 million (2001: £109 million) after tax.

The key assumptions used in determining the value of policies in force are:

	2002	2001
	%	%
Risk discount rate (net of tax)	**10.0**	10.0
Economic assumptions (gross of tax)		
Investment return on unit-linked funds	**6.8**	7.1
Investment return on non-linked funds	**5.0**	5.0
Expense inflation	**3.7**	3.7

The composition of the net tangible assets relating to long-term assurance funds is analysed as follows:

	2002	2001
	£m	£m
Loans and advances to banks	**135**	193
Debt securities	**871**	813
Equity shares	**1,626**	1,708
Other assets	**694**	757
Prepayments and accrued income	**21**	16
Other liabilities	**(84)**	(67)
Long-term assurance net assets attributable to policyholders	**3,263**	3,420

25 Deposits by banks

	group		*bank*	
	2002	2001	**2002**	2001
	£m	£m	**£m**	£m
Repayable on demand	**8,358**	7,204	**4,892**	6,013
With agreed maturity dates or periods of notice by remaining maturity				
— 3 months or less but not repayable on demand	**12,901**	17,948	**13,123**	14,232
— 1 year or less but over 3 months	**2,317**	2,430	**941**	993
— 5 years or less but over 1 year	**387**	784	**273**	350
— over 5 years	**436**	413	**833**	43
	24,399	28,779	**20,062**	21,631
Amounts include:				
Due to subsidiary undertakings			**8,022**	5,817
Due to fellow subsidiary undertakings	**3,042**	5,055	**643**	3,517

Notes on the Accounts (continued)

26 Customer accounts

	group		bank	
	2002	2001	**2002**	2001
	£m	£m	**£m**	£m
Repayable on demand	**77,813**	67,341	**55,287**	49,534
With agreed maturity dates or periods of notice by remaining maturity				
— 3 months or less but not repayable on demand	**45,972**	44,926	**21,128**	20,320
— 1 year or less but over 3 months	**3,750**	3,850	**1,366**	1,685
— 5 years or less but over 1 year	**2,608**	2,382	**1,565**	1,860
— over 5 years	**692**	387	**424**	328
	130,835	118,886	**79,770**	73,727
Amounts include:				
Due to joint ventures	**261**	229	**248**	217
Due to associates	**3**	3	**3**	3
Due to subsidiary undertakings			**1,329**	1,022
Due to fellow subsidiary undertakings	**86**	1,676	**826**	748
Due to parent undertaking	**2,593**	2,005	**1,344**	2,005

27 Debt securities in issue

	group		bank	
	2002	2001	**2002**	2001
	£m	£m	**£m**	£m
Bonds and medium-term notes, by remaining maturity				
— within 1 year	**1,414**	1,022	**796**	678
— between 1 and 2 years	**508**	1,286	**5**	832
— between 2 and 5 years	**1,657**	1,453	**847**	884
— over 5 years	**199**	217	**20**	97
	3,778	3,978	**1,668**	2,491
Other debt securities in issue, by remaining maturity				
— 3 months or less	**3,833**	3,425	**1,202**	967
— 1 year or less but over 3 months	**390**	493	**1**	122
— 5 years or less but over 1 year	**295**	580	**2**	3
— over 5 years	**47**	98	**—**	—
	4,565	4,596	**1,205**	1,092
	8,343	8,574	**2,873**	3,583

28 Other liabilities

	group		bank	
	2002	2001	**2002**	2001
	£m	£m	**£m**	£m
Short positions in securities:				
Debt securities				
— government securities	**5,769**	3,708	**3,368**	2,393
— other debt securities	**1,157**	854	**834**	277
Equity shares	**905**	—	**844**	—
	7,831	4,562	**5,046**	2,670
Liabilities, including losses, resulting from off-balance-sheet interest rate, exchange rate and equities contracts that are marked to market	**10,723**	6,899	**7,463**	5,873
Current taxation	**567**	353	**343**	172
Obligations under finance leases	**167**	160	**—**	3
Dividend payable	**507**	913	**507**	913
Long-term assurance liabilities attributable to policyholders (Note 24)	**3,263**	3,420	**—**	—
Other liabilities	**3,731**	3,376	**1,245**	1,245
	26,789	19,683	**14,604**	10,876
Liabilities, including losses, resulting from off-balance-sheet interest rate, exchange rate and equities contracts that are marked to market, include amounts:				
Due to subsidiary undertakings			**336**	107
Due to fellow subsidiary undertakings	**1,437**	838	**1,291**	801
Obligations under finance leases fall due, as follows				
— within 1 year	**—**	2	**—**	5
— between 1 and 5 years	**—**	2	**—**	—
— over 5 years	**367**	378	**—**	—
	367	382	**—**	5
— less future finance charges	**(200)**	(222)	**—**	(2)
	167	160	**—**	3

	group		bank	
	2002	2001	**2002**	2001
	£m	£m	**£m**	£m
Short positions in debt securities are in respect of securities				
— due within 1 year	**683**	242	**347**	233
— due 1 year and over	**6,243**	4,320	**3,855**	2,437
	6,926	4,562	**4,202**	2,670
— listed	**2,670**	1,942	**2,667**	1,935
— unlisted	**4,256**	2,620	**1,535**	735
	6,926	4,562	**4,202**	2,670

Notes on the Accounts (continued)

29 Provisions for liabilities and charges

a *Deferred taxation*

	group	*bank*
	£m	**£m**
At 1 January 2002*	**480**	**(75)**
Charge to the profit and loss account (Note 7)	**105**	**30**
Acquisitions	**(31)**	**(63)**
Exchange and other movements	**(21)**	**1**
At 31 December 2002	**533**	**(107)**

	group		*bank*	
	2002	2001*	**2002**	2001*
	£m	£m	**£m**	£m
Included in 'Provisions for liabilities and charges'	**588**	537	**60**	12
Included in 'Other assets' (Note 24)	**(55)**	(57)	**(167)**	(87)
	533	480	**(107)**	(75)

	group		*bank*	
	2002	2001*	**2002**	2001*
	£m	£m	**£m**	£m
Short-term timing differences	**(64)**	16	**(68)**	(13)
Accelerated capital allowances	**85**	83	**86**	81
Leasing transactions	**678**	603	**—**	—
Provisions for bad and doubtful debts	**(164)**	(176)	**(109)**	(128)
Relief for tax losses	**(17)**	(40)	**—**	—
Other items	**15**	(6)	**(16)**	(15)
	533	480	**(107)**	(75)

* *Figures for 2001 have been restated to reflect the adoption of Financial Reporting Standard 19, 'Deferred Tax', details of which are set out in Note1(d) on the Accounts on page 64.*

There is no material deferred taxation liability not provided for.

At 31 December 2002, there were potential future tax benefits of approximately £119 million (2001: £142 million) in respect of capital losses that have not been recognised because recoverability of the potential benefits is not considered likely.

No provision has been made for deferred taxation on gains recognised on revaluing property to its market value or on the sale of properties where potentially taxable gains will be covered by available tax losses.

29 Provisions for liabilities and charges *(continued)*

b *Other provisions for liabilities and charges*

	Provisions for pensions and other post-retirement obligations	*Provisions for contingent liabilities and commitments*	*Premises-related provisions*	*Insurance and other provisions*	*Total*
	£m	**£m**	**£m**	**£m**	**£m**
group					
At 1 January 2002	**263**	**150**	**99**	**246**	**758**
Additional provisions/increase in provisions	**19**	**48**	**34**	**167**	**268**
Provisions released	**—**	**(21)**	**(12)**	**(8)**	**(41)**
Acquisitions	**88**	**19**	**4**	**34**	**145**
Provisions utilised	**(29)**	**(45)**	**(11)**	**(44)**	**(129)**
Exchange and other movements	**(2)**	**27**	**3**	**8**	**36**
At 31 December 2002	**339**	**178**	**117**	**403**	**1,037**
bank					
At 1 January 2002	**101**	**53**	**94**	**2**	**250**
Additional provisions/increase in provisions	**10**	**17**	**31**	**3**	**61**
Provisions released	**—**	**—**	**(12)**	**—**	**(12)**
Acquisitions	**—**	**—**	**—**	**29**	**29**
Provisions utilised	**(5)**	**(32)**	**(9)**	**(1)**	**(47)**
Exchange and other movements	**7**	**—**	**6**	**19**	**32**
At 31 December 2002	**113**	**38**	**110**	**52**	**313**

Included within 'Provisions for contingent liabilities and commitments' are provisions for the costs of possible redress relating to the sales of certain personal pension plans and endowments of £19 million (2001: £37 million). The personal pension provision is the result of an actuarial calculation, extrapolated from a sample of cases and the timing of the expenditure depends on settlement of the individual claims.

The 'Premises-related provisions' relate to discounted future costs associated with vacant and sub-let short leasehold properties, including those that have or will become vacant as a consequence of the move of the group's head office and most of its London-based operations to Canary Wharf in 2002, and to discounted future costs to make good dilapidations upon the expiry of leases. The provisions cover rent voids while finding new tenants, shortfalls in expected rent receivable compared to rent payable and costs of refurbishing the building to attract tenants or make good dilapidations. Uncertainties relate to movements in market rents, the delay in finding new tenants, timing of rental reviews and the estimation of costs of refurbishment.

Included within 'Insurance and other provisions' are provisions of £271 million (2001: £184 million) relating to the general insurance provision.

Notes on the Accounts (continued)

30 Subordinated liabilities

	2002	2001
	£m	£m
Undated subordinated loan capital		
— bank	**1,262**	1,369
— subsidiary undertakings	**112**	118
	1,374	1,487
Dated subordinated loan capital		
— bank	**2,396**	2,297
— subsidiary undertakings	**460**	651
	2,856	2,948
Total subordinated liabilities		
— bank	**3,658**	3,666
— subsidiary undertakings	**572**	769
	4,230	4,435
Dated subordinated loan capital is repayable		
— within 1 year	**73**	61
— between 1 and 2 years	**328**	53
— between 2 and 5 years	**795**	965
— over 5 years	**1,660**	1,869
	2,856	2,948

Undated subordinated loan capital

		2002	2001
		£m	£m
bank			
US$750 million	Undated Floating Rate Primary Capital Notes	**466**	517
US$500 million	Undated Floating Rate Primary Capital Notes	**310**	345
US$300 million	Undated Floating Rate Primary Capital Notes (Series 3)	**186**	207
£150 million	9.25% Step-up Undated Subordinated Notes	**150**	150
£150 million	8.625% Step-up Undated Subordinated Notes	**150**	150
		1,262	1,369
subsidiary undertakings			
¥10,000 million	Undated Subordinated Variable Rate Medium Term Notes	**52**	53
Other undated subordinated liabilities individually less than £50 million		**60**	65
		112	118

The undated subordinated loan capital of the bank has characteristics which renders it similar in certain circumstances to preference shares. These borrowings are unsecured obligations of the bank. Claims in respect of principal and interest are subordinated to the claims of all creditors of the bank, other than claims of any creditors in respect of subordinated indebtedness ranking *pari passu* or junior to claims in respect of undated subordinated loan capital.

30 Subordinated liabilities *(continued)*

Dated subordinated loan capital

		2002 £m	2001 £m
bank			
US$400 million	8.625% Subordinated Notes 2004	**248**	276
£200 million	9% Subordinated Notes 2005	**200**	200
US$500 million	7.625% Subordinated Notes 2006	**310**	345
£100 million	14% Subordinated Unsecured Loan Stock 2002/2007	**—**	100
US$50 million	Subordinated Step-up Coupon Callable Floating Rate Notes 2007	**—**	34
£150 million	Subordinated Step-up Coupon Floating Rate Notes 2007	**—**	150
US$375 million	Subordinated Step-up Coupon Floating Rate Notes 2009	**232**	258
US$300 million	6.95% Subordinated Notes 2011	**186**	207
£350 million	Callable Subordinated Variable Coupon Notes 2017	**350**	—
£300 million	6.5% Subordinated Notes 2023	**298**	298
US$300 million	7.65% Subordinated Notes 2025	**186**	206
£225 million	6.25% Subordinated Notes 2041	**223**	223
		2,233	2,297
Amounts owed to parent undertaking			
€250 million	Floating Rate Subordinated Loan 2015	**163**	—
		2,396	2,297
Amounts owed to subsidiary undertaking			
€1,000 million	Floating Rate Subordinated Loan 2012	**651**	611
€900 million	7.75% Non-cumulative Subordinated Notes 2040	**586**	550
		3,633	3,458
subsidiary undertakings			
US$81 million	Subordinated Floating Rate Notes 2005	**50**	56
€152 million	Subordinated Callable Floating Rate Notes 2008	**99**	93
Other dated subordinated liabilities individually less than £50 million		**311**	213
		460	362
Amounts owed to fellow subsidiary undertaking			
US$300 million	Term Subordinated Debt 2011	**—**	207
Other dated subordinated liabilities individually less than £50 million		**—**	82
		460	651

The dated subordinated loan capital of the bank represents unsecured obligations of the bank. Claims in respect of principal and interest are subordinated to the claims of all creditors of the bank, other than claims of any creditors in respect of subordinated indebtedness ranking *pari passu* or junior to claims in respect of dated subordinated loan capital.

Interest rates on floating rate subordinated loan capital are related to interbank offered rates. On the remaining subordinated loan capital, interest is payable at fixed rates up to 9.25 per cent.

Generally, subordinated loan capital is repayable at par on maturity, but some is repayable prior to maturity at the option of the borrower, subject to the prior consent of the Financial Services Authority. The US$300 million 7.65% Subordinated Notes 2025 are repayable in May 2007 at par at the option of the holders.

Notes on the Accounts (continued)

30 Subordinated liabilities *(continued)*

The interest rate on the 9.25% Step-up Undated Subordinated Notes changes in December 2006 to become, for each successive five-year period, the rate per annum which is the sum of the yield on the then five-year benchmark UK gilt plus 2.15 per cent. The interest rate on the 8.625% Step-up Undated Subordinated Notes changes in December 2007 to become, for each successive five-year period, the rate per annum which is the sum of the yield on the then five-year benchmark UK gilt plus 1.87 per cent. In both cases, the issues are then repayable at the option of the borrower, subject to the prior consent of the Financial Services Authority.

The interest rates on the Subordinated Step-up Coupon Floating Rate Notes 2009 and the Floating Rate Subordinated Loan 2015 increase by 0.50 per cent five years prior to their maturity dates. In both cases, the issues are then repayable at the option of the borrower, subject to the prior consent of the Financial Services Authority.

The interest rate on the Callable Subordinated Variable Coupon Notes 2017 changes five years prior to its maturity date to become the rate per annum which is the sum of the yield on the then five-year benchmark UK gilt plus 1.70 per cent. The issue is then repayable at the option of the borrower, subject to the prior consent of the Financial Services Authority.

31 Minority interests — non-equity

		2002	2001
		£m	£m
€900 million	First capital contribution	**586**	550
€1,000 million	Second capital contribution	**651**	611
		1,237	1,161

HSBC Capital Funding 1 (UK) Limited Partnership was established by a subsidiary undertaking of the bank as General Partner, and a fellow subsidiary undertaking of HSBC Holdings plc, as Limited Partner.

The Limited Partner's first capital contribution of €900 million qualifies as innovative tier 1 capital for both the bank and the group on a consolidated basis. The proceeds of the first capital contribution were on-lent by the Limited Partnership to the bank's Paris branch by issue of 7.75% Non-cumulative Subordinated Notes 2040. The Notes may be redeemed at the option of the bank's Paris branch on the interest payment date in October 2010, or any interest payment date thereafter, subject to the prior consent of the Financial Services Authority.

The Limited Partner made a second capital contribution to the Limited Partnership of €1,000 million by way of assignment to the Limited Partnership of a €1,000 million Floating Rate Subordinated Loan 2012 made by the Limited Partner to the bank's Paris branch. The Limited Partner's second capital contribution qualifies as tier 2 capital for both the bank and the group on a consolidated basis. The interest rate on the Floating Rate Subordinated Loan 2012 is related to interbank offered rates, and the Loan is repayable at par on maturity, and also at the option of the bank's Paris branch on the interest payment date in October 2007, or any interest payment date thereafter, subject to the prior consent of the Financial Services Authority.

The Limited Partner's profit share for each distribution period is calculated as i) the lower of a) the amount of interest received by the Limited Partnership in respect of the Floating Rate Subordinated Loan 2012 and b) the profit of the Limited Partnership available for that distribution period, and ii) the lower of a) €69,750,000 and b) the profit of the Limited Partnership available for that distribution period less amounts paid under i).

There are limitations on the payment of the Limited Partner's profit share if the bank is prohibited under UK banking regulations or other requirements from paying distributions on its Parity Obligations, or if the bank has insufficient distributable reserves.

31 Minority interests — non-equity *(continued)*

The Limited Partnership will only be dissolved upon the occurrence of i) the redemption of the €900 million 7.75% Non-cumulative Subordinated Notes 2040, provided certain redemption conditions are satisfied, or ii) the passing of a resolution for the winding-up of the bank. In the event of a dissolution of the Limited Partnership, before any substitution event (see below), the Limited Partner shall be entitled to receive a) the Limited Partner's share of the €1,000 million Floating Rate Subordinated Loan 2012 (if any) and b) the liquidating distribution to which the Limited Partner is entitled in respect of its €900 million capital contribution, which amount shall not exceed the amount per security that would have been paid as the liquidating distribution from the assets of the bank had the Limited Partner's interest in the Limited Partnership been substituted by the Substitute Securities (see below).

If i) the total capital ratio of the bank or the group, on a consolidated basis, has fallen below the regulatory minimum ratio required, or ii) in view of the bank's deteriorating financial condition, the bank's Board of Directors expect i) to occur in the near term, then the Limited Partner's interest in the Limited Partnership, in respect of its first €900 million capital contribution, shall be substituted with fully paid ordinary shares issued by the bank ('Substitute Securities') and, as to the remainder, with an appropriate portion of the Floating Rate Subordinated Loan 2012.

32 Called up share capital

	Non-cumulative preference shares of £1 each	*Non-cumulative preference shares of US$0.01 each*	*Ordinary shares of £1 each*	*Total*
At 31 December 2001 and 2002	£m	£m	£m	£m
Authorised share capital	150	2	1,000	1,152
Issued, allotted and fully paid share capital	—	—	797	797

The issued, allotted and fully paid share capital of the bank comprises 796,969,095 ordinary shares of nominal value £1 each; 35,000,000 Third US$ non-cumulative preference shares of nominal value US$0.01 each; and one preferred ordinary share of nominal value £1.

The bank issued the following ordinary shares of nominal value £1 each during the year, all of which are held by HSBC Holdings plc:

	Ordinary shares of £1 each	*Share premium*
	£	£
1 July 2002	1	255,999,999
30 November 2002	65,884	1,250,796

The July issue of shares was in respect of the acquisition of HSBC Republic Bank (UK) Limited and the November issue was in respect of the acquisition of the business of the Madrid branch of HSBC Investment Bank plc.

On 7 March 2002, the bank redeemed its Series 1 and Series 2 Second preference shares at a redemption price of US$20 per Series 1 and US$5 per Series 2 Second preference share.

On 7 March 2002, the bank issued a further 2,000,000 Third preference shares to HSBC Holdings plc at an issue price of US$25 per share, where the nominal value was US$0.01 and the premium on issue was US$24.99 per share. The shares are redeemable at the option of the bank, on or after 8 March 2007, at a redemption price of US$25 per share. Dividends on Third preference shares are payable annually on 31 October at a rate of 7.5 per cent per annum, with the first dividend paid on 31 October 2002.

Notes on the Accounts (continued)

32 Called up share capital *(continued)*

In the event of a winding-up, Third preference shareholders would receive, in priority to the ordinary shareholders of the bank, repayment of US$25 per share, plus an amount equal to any dividends declared but unpaid in respect of the previous dividend for the period and any accrued and unpaid dividends for the period to the date of the commencement of winding-up. With the exception of the above, the preference shares do not carry any right to participate in any surplus of assets on a winding-up.

Holders of Third preference shares are not entitled to vote at general meetings of the shareholders, except in certain limited circumstances, such as the variation of the rights attaching to those shares, or in the event of a reduction of the preference share capital. In addition, Third preference shareholders are entitled to vote at general meetings of the shareholders if any resolution is proposed for a winding-up or sale of the whole business of the bank, or in the event of a failure to pay in full the dividend payable on the Third preference shares for the most recent dividend period.

33 Reserves

	group	*bank*	*Joint ventures and associates*
	£m	**£m**	**£m**
Share premium account			
At 1 January 2002	**12,009**	**12,009**	**—**
New share capital subscribed	**292**	**292**	**—**
Share capital redeemed	**(35)**	**(35)**	**—**
Exchange movements	**(58)**	**(58)**	**—**
At 31 December 2002	**12,208**	**12,208**	**—**
Revaluation reserves			
At 1 January 2002 (as previously reported)	**166**	**768**	**—**
Prior year adjustment*	—	**21**	**—**
At 1 January 2002	**166**	**789**	**—**
Realisation on disposal of properties	**(6)**	**—**	**—**
Unrealised deficit on revaluation of freehold and long leasehold properties	**(44)**	**(31)**	**—**
Net decrease in attributable net assets of subsidiary and associates	**—**	**(73)**	**—**
Exchange movements	**5**	**—**	**—**
At 31 December 2002	**121**	**685**	**—**
Profit and loss account			
At 1 January 2002 (as previously reported)	**2,658**	**2,056**	**26**
Prior year adjustment*	**18**	**(3)**	—
At 1 January 2002	**2,676**	**2,053**	**26**
Retained profit/(loss) for the year	**235**	**710**	**(7)**
Realisation on disposal of properties	**6**	**—**	**—**
Realisation on disposal of subsidiary and associates	**—**	**—**	**(11)**
Exchange and other movements	**412**	**2**	**—**
At 31 December 2002	**3,329**	**2,765**	**8**

* *Figures for 2001 have been restated to reflect the adoption of Financial Reporting Standard 19, 'Deferred Tax', details of which are set out in Note 1(d) on the Accounts on page 64.*

33 Reserves *(continued)*

Cumulative goodwill amounting to £84 million (2001: £84 million) has been charged against reserves in respect of acquisitions prior to 1 January 1998.

The reserves of the bank include distributable reserves of £2,750 million (2001: £2,038 million, after restating for FRS19, details of which are set out in Note 1 (d) on the Accounts on page 64).

Some of the group's banking subsidiary undertakings operate under local regulatory jurisdictions which could potentially restrict the amount of reserves that can be remitted to the bank in order to maintain local regulatory capital ratios.

Advantage has been taken of the exemptions applicable to Inland Revenue approved SAYE share option schemes and equivalent overseas schemes under Urgent Issues Task Force Abstract 17 (revised 2000) 'Employee share schemes'.

34 Analysis of total assets and total liabilities

a *Assets subject to sale and repurchase transactions*

	group		*bank*	
	2002 **£m**	2001 £m	**2002** **£m**	2001 £m
Total assets subject to sale and repurchase transactions	**4,254**	4,796	**1,464**	2,281

b *Assets leased to customers*

Amounts relating to assets leased to customers are included under the following balance sheet headings:

	2002 **£m**	2001 £m
Loans and advances to customers		
— finance leases	**2,525**	2,311
— hire purchase contracts	**984**	818
Tangible fixed assets		
— equipment on operating leases	**2,026**	1,837
	5,535	4,966

The cost of assets acquired during 2002 for letting under finance leases and hire purchase contracts by the group amounted to £466 million (2001: £611 million) and £475 million (2001: £427 million), respectively.

c *Assets charged as security for liabilities*

Assets have been pledged as security for liabilities included under the following headings:

	group		*bank*	
	2002 **£m**	2001 £m	**2002** **£m**	2001 £m
Deposits by banks	**910**	171	**892**	171
Customer accounts	**1,396**	75	**1,395**	75
Debt securities in issue	**158**	152	**111**	106
Other liabilities	**695**	—	**503**	—
	3,159	398	**2,901**	352

34 Analysis of total assets and total liabilities *(continued)*

c *Assets charged as security for liabilities (continued)*

The total assets pledged to secure the above liabilities are as follows:

	group		*bank*	
	2002	2001	**2002**	2001
	£m	£m	**£m**	£m
Assets pledged to secure liabilities	**11,320**	9,869	**10,431**	9,407

The above amounts are mainly made up of items included in 'Debt securities' of £9,675 million (2001: £9,253 million) for the group and £8,859 million (2001: £8,861 million) for the bank.

35 Financial instruments

a *Derivatives*

The group's derivatives are discussed in the 'Financial Review' on pages 35 to 38.

i Derivatives used for trading purposes

The following tables summarise the contract amount, replacement cost and mark-to-market values of third-party and internal trading derivatives by product type. The replacement cost shown is the positive mark-to-market value and represents the accounting loss the group would incur if the counterparty to a derivative contract failed to perform according to the terms of the contract and the collateral, if any, for the amount due proved to be of no value.

The notional or contractual amounts of these instruments indicate the volume of transactions outstanding at the balance sheet date; they do not represent amounts at risk.

Because all derivative instruments used for trading purposes are marked to market, carrying values are equal to mark-to-market values. Mark-to-market values are determined by reference to market rates prevailing on the date of valuation or by discounting future cash flows and include netted internal positions, except where otherwise indicated.

Netting is applied where a legal right of set-off exists. Mark-to-market assets and liabilities are presented gross, with allowable netting shown separately.

35 Financial instruments *(continued)*

a *Derivatives (continued)*

i *Derivatives used for trading purposes (continued)*

	2002		2001	
	Contract amount	*Replacement cost* [1]	*Contract amount*	*Replacement cost* [1]
	£m	**£m**	£m	£m
Spot and forward foreign exchange	**217,951**	**4,455**	233,601	2,851
Currency swaps, futures and options purchased	**72,079**	**1,729**	59,819	1,519
Currency options written	**33,122**	**—**	24,282	—
Other contracts	**3,970**	**71**	1,281	13
Total exchange rate contracts	**327,122**	**6,255**	318,983	4,383
Interest rate swaps	**590,756**	**10,358**	501,954	5,806
Interest rate futures, forward rate agreements, collars and options purchased	**126,446**	**761**	176,371	481
Interest rate options written	**42,448**	**—**	24,291	—
Total interest rate contracts	**759,650**	**11,119**	702,616	6,287
Equities, futures and options purchased	**16,764**	**1,007**	10,759	743
Equities options written	**11,741**	**—**	8,773	—
Total equities contracts	**28,505**	**1,007**	19,532	743
Netting		**(9,322)**		(4,566)
Total	**1,115,277**	**9,059**	1,041,131	6,847

[1] *Third-party contracts only*

'Other contracts' in the table above includes third party credit derivatives with a contract amount of £3,850 million (2001: £1,209 million) and a replacement cost of £70 million (2001: £12 million). These amounts represent mainly credit default protection products bought or sold.

	2002	2001
	Mark-to-market values	*Mark-to-market values*
	£m	£m
Exchange rate		
— assets	**6,646**	4,403
— liabilities	**(6,987)**	(4,295)
Interest rate		
— assets	**11,199**	6,310
— liabilities	**(11,716)**	(6,525)
Equities		
— assets	**1,007**	743
— liabilities	**(1,342)**	(645)
Total		
— assets	**18,852**	11,456
— liabilities	**(20,045)**	(11,465)
Netting	**(9,322)**	(4,566)

35 Financial instruments *(continued)*

a *Derivatives (continued)*

i *Derivatives used for trading purposes (continued)*

Included in the amounts in the previous table is cash collateral meeting the offset criteria as follows:

	2002	2001
	£m	£m
Offset against assets	**709**	168
Offset against liabilities	**28**	52

ii *Derivatives used for risk management purposes*

The majority of the transactions undertaken for risk management purposes are between business units within the group, one of which is a trading desk, which may then lay off the resulting position by trading in the external market. Internal positions are integral to the group's asset and liability management and are included within analyses of non-trading positions in the tables below.

The table below summarises the contract amount and replacement cost of derivatives used for risk management purposes by product type. The replacement cost shown represents the accounting loss the group would incur if the counterparty to a derivative contract failed to perform according to the terms of the contract and the collateral, if any, for the amount due proved to be of no value.

	2002		2001	
	Contract amount	*Replacement cost*[1]	*Contract amount*	*Replacement cost*[1]
	£m	**£m**	£m	£m
Spot and forward foreign exchange	**11,913**	**1**	9,278	—
Currency swaps, futures and options purchased	**4,772**	**24**	2,072	25
Total exchange rate contracts	**16,685**	**25**	11,350	25
Interest rate swaps	**125,381**	**313**	98,119	222
Interest rate futures, forward rate agreements and options purchased	**1,355**	**1**	3,151	2
Total interest rate contracts	**126,736**	**314**	101,270	224

1 *Third-party contracts only*

The table below summarises the carrying value and mark-to-market value of derivative contracts held for risk management purposes. Mark-to-market values for assets and liabilities arising from derivatives held for non-trading purposes are determined in the same way as those set out for trading derivatives above including internal positions.

	2002		2001	
	Carrying value	*Mark-to-market values*	*Carrying value*	*Mark-to-market values*
	£m	**£m**	£m	£m
Exchange rate				
— assets	**7**	**40**	21	87
— liabilities	**(298)**	**(558)**	(27)	(46)
Interest rate				
— assets	**610**	**2,710**	591	1,642
— liabilities	**(268)**	**(1,900)**	(328)	(1,130)

35 Financial instruments *(continued)*

b *Other financial instruments*

i *Financial instruments held for trading purposes*

	2002	2001
	Mark-to-market values	*Mark-to-market values*
	£m	£m
Assets		
Treasury bills and other eligible bills	**469**	15
Loans and advances to banks and customers	**14,140**	11,328
Debt securities	**24,377**	22,683
Equity shares	**1,917**	823
	40,903	34,849
Liabilities		
Short positions in securities	**7,831**	4,562
Debt securities in issue	**81**	113
Deposits by banks and customer accounts	**10,830**	8,889
	18,742	13,564

The net trading assets above are funded by liabilities whose fair value is not materially different from their carrying value.

ii *Financial instruments not held for trading purposes and for which a liquid and active market exists*

	2002		2001	
	Carrying value	*Mark-to-market values*	*Carrying value*	*Mark-to-market values*
	£m	**£m**	£m	£m
Assets				
Treasury bills and other eligible bills	**1,578**	**1,582**	2,922	2,929
Debt securities	**20,571**	**21,053**	19,194	19,328
Equity shares	**1,566**	**1,763**	1,464	1,549
	23,715	**24,398**	23,580	23,806
Liabilities				
Debt securities in issue	**3,223**	**3,202**	8,461	8,467
Subordinated liabilities	**3,847**	**3,903**	4,435	4,409
	7,070	**7,105**	12,896	12,876

Where possible, mark-to-market values have been estimated using market prices for these financial instruments. Where market prices are not available, values have been estimated using quoted prices for financial instruments with similar characteristics, or otherwise using a suitable valuation technique where practicable to do so.

Notes on the Accounts (continued)

35 Financial instruments *(continued)*

b *Other financial instruments (continued)*

The valuation techniques used are:

— *Treasury bills and other eligible bills*

The mark-to-market value approximates to carrying value because these are mainly short-term in maturity with a carrying value not materially different from mark-to-market value.

— *Loans and advances to banks and customers*

For variable rate loans and advances with no significant change in credit risk, the carrying value is considered to represent mark-to-market value. The mark-to-market values of other loans and advances are estimated by discounting future cash flows using market interest rates.

— *Debt securities and equity shares*

Listed securities are valued at middle-market prices and unlisted securities at management's valuation, which takes into consideration future earnings streams, valuations of equivalent quoted securities and other relevant techniques.

— *Debt securities in issue, short positions in securities, subordinated liabilities and preference shares*

Mark-to-market values are estimated using quoted market prices at the balance sheet date.

— *Deposits by banks and customer accounts*

Deposits by banks and customer accounts that mature or re-price after six months are grouped by residual maturity. Fair value is estimated using discounted cash flows, applying either market rates, where applicable, or current rates offered for deposits of similar re-pricing maturities.

c *Gains and losses on hedges*

Gains and losses on instruments used for hedging are recognised in line with the underlying items that are being hedged. The unrecognised gains on instruments used for hedging as at 31 December 2002 were £1,814 million (2001: £1,580 million) and the unrecognised losses were £1,573 million (2001: £1,283 million).

Unrecognised gains of £784 million and unrecognised losses of £648 million are expected to be recognised in 2003.

Of the gains and losses included in the profit and loss account in 2002, £517 million gains and £418 million losses were unrecognised at 1 January 2002.

d *Liquidity management*

The group's liquidity management process is described in the 'Financial Review' section on pages 32 and 33.

36 Memorandum items and foreign exchange rate, interest rate and equities contracts

a *Contingent liabilities and commitments*

	2002			2001		
	Contract amount	*Credit equivalent amount*	*Risk-weighted amount*	*Contract amount*	*Credit equivalent amount*	*Risk-weighted amount*
	£m	**£m**	**£m**	£m	£m	£m
group						
Contingent liabilities						
Acceptances and endorsements	**742**	**502**	**391**	846	638	610
Guarantees and assets pledged as collateral security						
— guarantees and irrevocable letters of credit	**14,353**	**10,477**	**8,774**	13,379	9,651	7,821
— other	**6**	**6**	**6**	3	3	2
	15,101	**10,985**	**9,171**	14,228	10,292	8,433
Commitments						
Documentary credits and short-term trade-related transactions	**1,515**	**782**	**293**	1,403	690	298
Forward asset purchases and forward forward deposits placed	**70**	**70**	**77**	57	57	48
Undrawn note issuance and revolving underwriting facilities	**36**	**18**	**18**	157	78	78
Undrawn formal standby facilities, credit lines and other commitments to lend						
— over 1 year	**14,825**	**7,412**	**6,609**	12,592	6,296	5,500
— 1 year or less	**44,931**	**—**	**—**	36,468	—	—
	61,377	**8,282**	**6,997**	50,677	7,121	5,924

	2002	2001
	£m	£m
Incurred on behalf of parent and fellow subsidiary undertakings (contract amount)		
— contingent liabilities	**158**	145

36 Memorandum items and foreign exchange rate, interest rate and equities contracts *(continued)*

a *Contingent liabilities and commitments (continued)*

	2002			2001		
	Contract amount	*Credit equivalent amount*	*Risk-weighted amount*	*Contract amount*	*Credit equivalent amount*	*Risk-weighted amount*
	£m	**£m**	**£m**	£m	£m	£m
bank						
Contingent liabilities						
Acceptances and endorsements	**631**	**387**	**307**	810	601	577
Guarantees and assets pledged as collateral security						
— guarantees and irrevocable letters of credit	**8,423**	**6,500**	**5,073**	7,514	5,868	4,624
	9,054	**6,887**	**5,380**	8,324	6,469	5,201
Commitments						
Documentary credits and short-term trade-related transactions	**1,081**	**590**	**213**	1,282	652	270
Forward asset purchases and forward forward deposits placed	**16**	**16**	**12**	22	22	18
Undrawn formal standby facilities, credit lines and other commitments to lend						
— over 1 year	**9,938**	**4,969**	**4,366**	9,159	4,580	3,957
— 1 year or less	**39,434**	**—**	**—**	34,803	—	—
	50,469	**5,575**	**4,591**	45,266	5,254	4,245

	2002	2001
	£m	£m
Incurred on behalf of subsidiary undertakings (contract amount)		
— contingent liabilities	**46**	99
Incurred on behalf of parent and fellow subsidiary undertakings (contract amount)		
— contingent liabilities	**19**	58

The preceding tables give the nominal principal amounts, credit equivalent amounts and risk-weighted amounts of off-balance-sheet transactions. The credit equivalent amounts are calculated for the purposes of deriving the risk-weighted amounts. These are assessed in accordance with the Financial Services Authority's guidelines, which implement the Basel Capital Accord on capital adequacy and depend on the status of the counterparty and the maturity characteristics.

Contingent liabilities and commitments are credit-related instruments that include acceptances, letters of credit, guarantees and commitments to extend credit. The contractual amounts represent the amounts at risk should the contract be fully drawn upon and the client default. Since a significant portion of guarantees and commitments are expected to expire without being drawn upon, the total of the contract amounts is not representative of future liquidity requirements.

36 Memorandum items and foreign exchange rate, interest rate and equities contracts *(continued)*

b *Concentrations of contingent liabilities and commitments*

The group has the following concentration of exposure to contingent liabilities and commitments, based on the location of the office recording the transaction:

	United Kingdom	*Continental Europe*	*Rest of the world*	*Total*
	£m	£m	£m	£m
Contract amounts				
Contingent liabilities				
2002	**7,602**	**7,204**	**295**	**15,101**
2001	7,092	6,863	273	14,228
Commitments				
2002	**47,891**	**9,219**	**4,267**	**61,377**
2001	42,449	6,220	2,008	50,677

37 Market risk management

The group's market risk management process is discussed in the 'Financial Review' on pages 29 and 30 from the paragraph under the heading 'Market risk' to the paragraph ended 'impact of extreme events on the market risk exposures of the group'.

a *Trading Value at Risk (VAR)*

VAR is a technique that estimates the potential losses that could occur on risk positions taken due to movements in market rates and prices over a specified time horizon and to a given level of confidence.

Trading VAR for 2002 is set out below:

	At 31 December	*Minimum during the year*	*Maximum during the year*	*Average for the year*
	£m	**£m**	**£m**	**£m**
Total trading activities	**25.5**	**17.0**	**41.9**	**28.1**
Foreign exchange trading positions	**7.0**	**3.5**	**22.4**	**9.9**
Interest rate trading positions	**22.9**	**15.9**	**36.4**	**22.7**
Equities trading positions	**3.8**	**0.8**	**5.3**	**2.1**

Trading VAR for 2001 is set out below:

	At 31 December	*Minimum during the year*	*Maximum during the year*	*Average for the year*
	£m	£m	£m	£m
Total trading activities	27.5	13.5	59.4	22.4
Foreign exchange trading positions	6.9	3.2	12.6	6.9
Interest rate trading positions	25.0	11.2	53.3	19.5
Equities trading positions	2.3	0.7	6.9	2.4

The VAR noted for foreign exchange positions excludes structural foreign currency exposures, since related gains or losses are taken through reserves.

Notes on the Accounts (continued)

37 Market risk management *(continued)*

b *Interest rate sensitivity gap table*

In accordance with FRS 13, 'Derivatives and Other Financial Instruments', the table below discloses the mismatching of the dates on which interest receivable on assets and interest payable on liabilities are next reset to market rate on a contractual basis, or, if earlier, the dates on which the instruments mature. Actual reset dates may differ from contractual dates owing to prepayments and the exercise of options. In addition, contractual terms may not be representative of the behaviour of assets and liabilities. For these reasons, the group manages its interest rate risk on a different basis from that presented below, taking into account behavioural characteristics of the relevant assets and liabilities.

	Not more than three months	*More than three months but not more than six months*	*More than six months but not more than one year*	*More than one year but not more than five years*	*More than five years*	*Non-interest bearing*	*Trading book*	*Total*
2002	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Assets								
Treasury bills and other eligible bills	**1,257**	**93**	**60**	**168**	**—**	**—**	**469**	**2,047**
Loans and advances to banks	**16,037**	**960**	**956**	**202**	**157**	**326**	**7,989**	**26,627**
Loans and advances to customers	**74,940**	**3,665**	**3,633**	**10,812**	**3,863**	**1,843**	**6,151**	**104,907**
Debt securities and equity shares	**7,682**	**1,005**	**2,961**	**4,223**	**4,688**	**1,578**	**26,294**	**48,431**
Other assets	**1,377**	**—**	**—**	**—**	**—**	**25,083**	**9,906**	**36,366**
Internal funding of the trading book	**17,764**	**1,817**	**546**	**1,234**	**37**	**(197)**	**(21,201)**	**—**
Total assets	**119,057**	**7,540**	**8,156**	**16,639**	**8,745**	**28,633**	**29,608**	**218,378**
Liabilities								
Deposits by banks	**16,144**	**513**	**1,041**	**165**	**150**	**1,839**	**4,547**	**24,399**
Customer accounts	**104,899**	**1,811**	**979**	**254**	**364**	**16,245**	**6,283**	**130,835**
Debt securities in issue	**3,493**	**482**	**45**	**3,010**	**245**	**987**	**81**	**8,343**
Other liabilities	**146**	**—**	**—**	**147**	**19**	**13,528**	**18,697**	**32,537**
Loan capital and other subordinated liabilities	**554**	**841**	**323**	**1,179**	**1,333**	**—**	**—**	**4,230**
Minority interests and shareholders' funds	**—**	**—**	**—**	**—**	**—**	**18,034**	**—**	**18,034**
Total liabilities	**125,236**	**3,647**	**2,388**	**4,755**	**2,111**	**50,633**	**29,608**	**218,378**
Net on-balance-sheet items	**(6,179)**	**3,893**	**5,768**	**11,884**	**6,634**	**(22,000)**	**—**	**—**
Off-balance-sheet items	**(14,440)**	**(730)**	**3,260**	**13,049**	**(1,139)**	**—**	**—**	**—**
Interest rate sensitivity gap	**(20,619)**	**3,163**	**9,028**	**24,933**	**5,495**	**(22,000)**	**—**	**—**
Cumulative interest rate sensitivity gap	**(20,619)**	**(17,456)**	**(8,428)**	**16,505**	**22,000**	**—**	**—**	**—**

37 Market risk management *(continued)*

b *Interest rate sensitivity gap table (continued)*

2001*	*Not more than three months* £m	*More than three months but not more than six months* £m	*More than six months but not more than one year* £m	*More than one year but not more than five years* £m	*More than five years* £m	*Non-interest bearing* £m	*Trading book* £m	*Total* £m
Assets								
Treasury bills and other eligible bills	2,406	437	64	15	—	—	15	2,937
Loans and advances to banks	20,967	1,526	899	260	155	1,036	7,488	32,331
Loans and advances to customers	59,877	6,538	4,604	9,402	3,191	1,549	3,840	89,001
Debt securities and equity shares	8,122	623	880	5,599	3,575	1,859	23,506	44,164
Other assets	948	—	—	—	—	25,635	7,293	33,876
Internal funding of the trading book	14,489	2,408	1,666	2,711	42	128	(21,444)	—
Total assets	106,809	11,532	8,113	17,987	6,963	30,207	20,698	202,309
Liabilities								
Deposits by banks	21,015	978	423	244	181	1,631	4,307	28,779
Customer accounts	93,206	1,755	901	641	354	17,447	4,582	118,886
Debt securities in issue	4,854	706	357	2,326	218	—	113	8,574
Other liabilities	51	—	—	148	11	12,676	11,696	24,582
Loan capital and other subordinated liabilities	1,363	471	193	934	1,474	—	—	4,435
Minority interests and shareholders' funds	—	—	—	—	—	17,053	—	17,053
Total liabilities	120,489	3,910	1,874	4,293	2,238	48,807	20,698	202,309
Net on-balance-sheet items	(13,680)	7,622	6,239	13,694	4,725	(18,600)	—	—
Off-balance-sheet items	(9,398)	1,029	1,338	7,640	(609)	—	—	—
Interest rate sensitivity gap	(23,078)	8,651	7,577	21,334	4,116	(18,600)	—	—
Cumulative interest rate sensitivity gap	(23,078)	(14,427)	(6,850)	14,484	18,600	—	—	—

** Figures for 2001 have been restated to reflect the adoption of Financial Reporting Standard 19, 'Deferred Tax', details of which are set out in Note 1(d) on the Accounts on page 64.*

A positive interest rate sensitivity gap exists where more assets than liabilities re-price during a given period. Although a positive gap position tends to benefit net interest income in a rising interest rate environment, the actual effect will depend on a number of factors, including the extent to which repayments are made earlier or later than the contracted date and variations in interest rates within re-pricing periods and among currencies. Similarly, a negative interest rate sensitivity gap exists where more liabilities than assets re-price during a given period. In this case, a negative gap position tends to benefit net interest income in a declining interest rate environment, but again the actual effect will depend on the same factors as for positive interest rate gaps, as described above.

Notes on the Accounts (continued)

37 Market risk management *(continued)*

c *Assets and liabilities denominated in foreign currency*

	group		bank	
	2002	2001*	**2002**	2001*
	£m	£m	**£m**	£m
Denominated in sterling	**94,820**	90,301	**90,152**	85,043
Denominated in currencies other than sterling	**123,558**	112,008	**51,173**	47,660
Total assets	**218,378**	202,309	**141,325**	132,703
Denominated in sterling	**101,134**	91,186	**89,224**	84,566
Denominated in currencies other than sterling	**117,244**	111,123	**52,101**	48,137
Total liabilities	**218,378**	202,309	**141,325**	132,703

** Figures for 2001 have been restated to reflect the adoption of Financial Reporting Standard 19, 'Deferred Tax', details of which are set out in Note 1(d) on the Accounts on page 64.*

d *Structural currency exposures*

The group's management of structural foreign currency exposures is disclosed in the 'Financial Review' on page 31 and 32.

The group's structural currency exposures as at the year-end were as follows:

2002

Functional currency of the operation involved	*Net investments in operations*	*Borrowing taken out in the functional currencies of operations in order to hedge the net investment in such operations*	*Remaining structural currency exposures*
	£m	**£m**	**£m**
Euro	**9,144**	**1,237**	**7,907**
US dollars	**1,201**	**549**	**652**
Swiss francs	**1,105**	**410**	**695**
Hong Kong dollars	**496**	**—**	**496**
Turkish lira	**274**	**—**	**274**
Maltese liri	**121**	**—**	**121**
Other	**47**	**—**	**47**
Total	**12,388**	**2,196**	**10,192**

2001

Functional currency of the operation involved	*Net investments in operations*	*Borrowing taken out in the functional currencies of operations in order to hedge the net investment in such operations*	*Remaining structural currency exposures*
	£m	£m	£m
Euro	8,859	1,161	7,698
US dollars	1,545	620	925
Swiss francs	832	369	463
Hong Kong dollars	582	—	582
Turkish lira	273	—	273
Maltese liri	106	—	106
Other	47	—	47
Total	12,244	2,150	10,094

38 Litigation

The bank and certain subsidiary undertakings are named in, and are defending, legal actions in various jurisdictions arising from their normal business. No material adverse impact on the financial position of the group is expected to arise from these proceedings.

39 Capital commitments

	group		*bank*	
	2002	2001	**2002**	2001
	£m	£m	**£m**	£m
Expenditure contracted for	**662**	327	**117**	128

40 Lease commitments

At 31 December 2002, the group was committed to various non-cancellable operating leases, which require aggregate future rental payments as follows:

	Leasehold land and buildings
	£m
Payable within 1 year	**98**
Payable between 1 and 2 years	**90**
Payable between 2 and 3 years	**84**
Payable between 3 and 4 years	**80**
Payable between 4 and 5 years	**74**
Payable in over 5 years	**568**
	994

At the year-end, annual commitments under non-cancellable operating leases were:

	group		*bank*	
	2002	2001	**2002**	2001
	£m	£m	**£m**	£m
Leasehold land and buildings				
Operating leases which expire				
— within 1 year	**2**	4	**1**	2
— between 1 and 5 years	**19**	18	**12**	11
— in over 5 years	**77**	77	**74**	72
	98	99	**87**	85

Notes on the Accounts (continued)

41 Segmental analysis

As the group is not required to disclose turnover, no segmental analysis of turnover is included. Turnover of non-banking businesses is included in 'other operating income' in the table below. The allocation of earnings reflects the benefit of shareholders' funds to the extent that these costs are actually allocated to businesses in the segment by way of intra-group capital and funding structures. Common costs are included in segments on the basis of the actual recharges made.

a *By geographical region*

In the analysis set out below, net assets include an appropriate amount of shareholders' funds, based on the proportion of risk-weighted assets in each segment. Geographical information has been classified by the location of the principal operations of the subsidiary undertaking or, in the case of the bank, by the location of the branch responsible for reporting the results or for advancing the funds.

	United Kingdom	*Continental Europe*	*Rest of the world*	*Total*
2002	**£m**	**£m**	**£m**	**£m**
Gross income				
Interest receivable	**5,366**	**2,539**	**379**	**8,284**
Dividend income	**94**	**20**	**—**	**114**
Fees and commissions receivable	**2,075**	**1,034**	**52**	**3,161**
Dealing profits	**191**	**135**	**62**	**388**
Other operating income	**464**	**68**	**18**	**550**
Total gross income	**8,190**	**3,796**	**511**	**12,497**
Profit/(loss) on ordinary activities before tax	**2,190**	**(52)**	**147**	**2,285**
Attributable profit/(loss)	**1,551**	**(309)**	**137**	**1,379**
Net assets	**10,393**	**5,895**	**167**	**16,455**
Total assets	**123,799**	**86,356**	**8,223**	**218,378**
2001*	£m	£m	£m	£m
Gross income				
Interest receivable	5,920	3,238	325	9,483
Dividend income	9	24	—	33
Fees and commissions receivable	1,966	813	27	2,806
Dealing profits	237	177	28	442
Other operating income	537	61	28	626
Total gross income	8,669	4,313	408	13,390
Profit on ordinary activities before tax	2,164	36	90	2,290
Attributable profit/(loss)	1,546	(161)	85	1,470
Net assets	10,048	5,455	145	15,648
Total assets	114,856	80,362	7,091	202,309

* *Figures for 2001 have been restated to reflect the adoption of Financial Reporting Standard 19, 'Deferred Tax', details of which are set out in Note1(d) on the Accounts on page 64.*

41 Segmental analysis *(continued)*

b *By class of business*

	2002 **£m**	2001* £m
Profit/(loss) on ordinary activities before tax		
UK Personal Banking	**555**	606
UK Commercial Banking	**627**	563
UK Corporate and Institutional Banking	**312**	494
UK Treasury and Capital Markets	**467**	338
Investment Banking	**(2)**	—
International Banking	**208**	193
CCF	**359**	371
Private Banking	**225**	185
HSBC Trinkaus & Burkhardt	**16**	—
Amortisation of goodwill	**(482)**	(460)
	2,285	2,290
Net assets		
UK Personal Banking	**1,366**	1,224
UK Commercial Banking	**1,081**	1,023
UK Corporate and Institutional Banking	**1,307**	1,386
UK Treasury and Capital Markets	**509**	614
Investment Banking	**346**	—
International Banking	**969**	630
CCF	**6,822**	7,437
Private Banking	**3,882**	3,334
HSBC Trinkaus & Burkhardt	**173**	—
	16,455	15,648
Total assets		
UK Personal Banking	**35,579**	30,724
UK Commercial Banking	**19,272**	17,752
UK Corporate and Institutional Banking	**19,107**	19,276
UK Treasury and Capital Markets	**45,681**	47,037
Investment Banking	**2,798**	—
International Banking	**13,489**	12,670
CCF	**49,220**	47,082
Private Banking	**26,122**	27,768
HSBC Trinkaus & Burkhardt	**7,110**	—
	218,378	202,309

* *Figures for 2001 have been restated to reflect the adoption of Financial Reporting Standard 19, 'Deferred Tax', details of which are set out in Note1(d) on the Accounts on page 64.*

The amortisation of goodwill includes £303 million (2001: £304 million) in respect of CCF and £169 million (2001: £147 million) in respect of Private Banking.

Notes on the Accounts (continued)

42 Related party transactions

a *Transactions, arrangements and agreements involving Directors and others*

Particulars of transactions, arrangements and agreements entered into by subsidiary undertakings of the bank with Directors and connected persons and companies controlled by them and with officers of the bank disclosed pursuant to section 232 of the Companies Act 1985 are as follows:

	2002		2001	
	Number	*£000*	*Number*	*£000*
Directors and connected persons and companies controlled by them:				
Loans and credit card transactions (including £64,000 in credit card transactions (2001: £42,000))	**18**	**91,465**	14	89,014
Officers:				
Loans and credit card transactions (including £78,000 in credit card transactions (2001: £106,000))	**22**	**6,986**	26	4,378

b *Joint ventures and associates*

Information relating to joint ventures and associates can be found in the Notes on the Accounts, where the following are disclosed:

— Note 14: amounts due from joint ventures and associates

— Note 19: interests in joint ventures

— Note 20: interests in associates

— Note 26: amounts due to joint ventures and associates

c *Transactions with other related parties of the group*

Pension funds

At 31 December 2002, the HSBC Bank (UK) Pension Scheme had deposits of £150 million (2001: £180 million) with the bank.

43 Subsequent event

As disclosed in Note 5(b), the HSBC Group has paid £500 million into the HSBC Bank (UK) Pension Scheme in anticipation of a shortfall arising on the triennial actuarial valuation.

44 Approval of the accounts

These accounts were approved by the Board of Directors on 3 March 2003.

45 Ultimate parent company

The ultimate parent company of the group is HSBC Holdings plc, which is incorporated in England.

HSBC Holdings plc is the only undertaking for which consolidated accounts that include the consolidated accounts of the group are drawn up.

HSBC Holdings plc is HSBC Bank plc's direct and ultimate controlling party as defined under Financial Reporting Standard 8, 'Related Party Disclosures'.

Copies of HSBC Holdings plc's *Annual Review 2002* and *Annual Report and Accounts 2002* can be obtained from its registered office at 8 Canada Square, London E14 5HQ, or on the HSBC Group's web site, www.hsbc.com.

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