

# HSBC Bank Australia Ltd

A.B.N. 48 006 434 162

**Annual Report and Accounts 2020**



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## Directors' report

The Directors of HSBC Bank Australia Limited (the 'Company' or the 'Bank') submit their report, together with the financial statements and related notes of the Company and its controlled entities (together the 'consolidated entity') for the financial year ended 31 December 2020 and the auditor's report thereon.

### Directors

The Directors of the Company at any time during or since the end of the financial year are:

Grant King, Non-executive Director (appointed Independent Non-executive Chairman 22 October 2020)

Graham Bradley AM, Independent Non-executive Chairman, (resigned 21 October 2020)

Carol Austin, Non-executive Director

Matthew Lobner, Non-executive Director

Kenneth Ng, Non-executive Director

Jann Skinner, Non-executive Director

Geoff Wilson, Non-executive Director

Kaber Mclean, Chief Executive Officer (appointed 1 March 2020)

Noel McNamara, Interim Chief Executive Officer (resigned 29 February 2020)

### Principal activities

The principal activities of the consolidated entity during the financial year were the provision of financial services comprising of lending, deposit taking, domestic and international trade finance, custodial securities services, global liquidity and cash management, money market services, interest rate and foreign currency trading and services, capital markets services and financial advice.

The Company is an Australian unlisted public limited company.

The registered office and principal place of business of the company is Level 36 International Tower One, 100 Barangaroo Avenue, Sydney NSW 2000.

### Review of operations

In 2020, the consolidated entity reported a profit from its continuing operations before income tax of \$315.0m, down from \$474.4m in 2019. Operating income before loan impairment charges decreased by 7.9% primarily due to the impacts of COVID-19 on the Australian economy, on both wholesale and retail portfolios. Operating costs remained relatively flat/low mainly on account of reduction in the performance related pay accrual and lower discretionary expenditure.

Total assets increased to \$47,036.3m driven by increases in customer advances and liquid asset holdings. Customer advances increased largely due to growth in the mortgage portfolio following a number of successful mortgage campaigns and expansion of the broker channel for mortgages.

### Dividends

Dividends paid or declared by the Company to shareholders since the end of the previous financial year were \$79.6m including payments on the Tier 1 instruments (2019: \$162.5m). Dividend payments were in line with the Bank's dividend policy.

### Significant changes in the state of affairs

The Bank continued to maintain a strong liquidity policy in line with local regulatory requirements and the HSBC Group, which together with a strong capital position, ensured that the Bank was able to effectively service its longstanding commitment to its

customers as well as maintaining its competitive position in the domestic market. In the opinion of the Directors, other than the impacts of COVID-19, there were no significant changes in the state of affairs of the Company or the consolidated entity during the period under review.

### Environmental regulation

The Company and its controlled entities are not subject to any particular or significant environmental regulation under a law of the Commonwealth or of a State or Territory.

### Events subsequent to reporting date

In the interval between the end of the financial year and the date of this report, no other item, transaction or event of a material and unusual nature has arisen that is likely, in the opinion of the Directors of the Company, to affect significantly the operations of the consolidated entity, the results of those operations, or the state of affairs of the consolidated entity, in current or future financial years.

### Likely developments

Information about likely developments in the operations of the consolidated entity and the expected results of those operations in future financial years has not been included in this report because disclosure of the information would be likely to result in unreasonable prejudice to the consolidated entity.

### Non-audit services

Details of the amounts paid to PricewaterhouseCoopers ('PwC') and its related practices for audit and non-audit services provided during the year are set out in note 7 of the financial statements.

During the financial year PwC has performed certain other services in addition to their statutory duties.

The Directors have considered the non-audit services provided during the financial year by PwC and are satisfied that the provision of those non-audit services by the Company's auditor is compatible with, and did not compromise, the auditor independence requirements of the Corporations Act 2001 for the following reasons:

- all non-audit assignments were approved in accordance with the process set out by the HSBC Group Audit Committee terms of reference on the agreed framework for engaging auditors for non-audit services; and
- none of the services undermine the general principles relating to auditor independence as set out in APES 110 *Code of Ethics for Professional Accountants*.

### Lead auditor's independence declaration

The lead auditor's independence declaration is set out on page 61 for the year ended 31 December 2020.

### Indemnification and insurance of Directors and officers

During the financial year, the consolidated entity paid premiums in respect of contracts insuring all the directors, executive officers and those acting in a capacity of an officer of the Company and its controlled entities against any liability incurred by them in their role as directors or executive officers of any entity, except where:

- the liability arises out of conduct involving a wilful breach of duty; or
- there has been a contravention of sections 182 and/or 183 of the Corporations Act 2001.

The Directors have not included details of the nature of liabilities covered or the amount of premium paid in respect of the directors' and officers' liability contracts, as such disclosure is prohibited under the terms of the contract.

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### Directors' benefits

No Director has, since the end of the previous financial year, received or become entitled to receive a benefit (other than a benefit included in the aggregate amount of remuneration received or due and receivable by them as shown in the consolidated financial statements) by reason of a contract made by the Company, a controlled entity or a related body corporate with the Director or with a firm in which the Director or a close member of their family (hereinafter, a 'Related Person') is a member, or with an entity in which the Director or a Related Person of any of them has a substantial interest, other than that disclosed in the financial statements.

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### Regulatory disclosures

Full details of the market disclosures and liquidity under Pillar 3 as required by Australian Prudential Standard 330 'Public Disclosure' are provided in the Regulatory Disclosures section of the Bank's website at [www.hsbc.com.au](http://www.hsbc.com.au).

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### Rounding off of amounts

The Company is of the kind referred to in ASIC Legislative Instrument 2016/191, relating to the 'rounding off' of amounts in the Directors' report. Amounts in this report and the accompanying financial statements have been rounded, where appropriate, to the nearest tenth of a million dollars except where otherwise stated.

The report is made with a resolution of the Directors.



**Grant King**  
Chairman

**Kaber Mclean**  
Director

Dated at Sydney this 15 February 2021

## Financial statements

### Income statements

for the year ended 31 December 2020

	Notes	Consolidated		Company	
		2020 \$m	2019 \$m	2020 \$m	2019 \$m
Interest income	4(i)	925.1	1,186.4	925.1	1,186.4
Interest expense	4(ii)	(214.2)	(432.0)	(214.2)	(432.0)
<b>Net interest income</b>		<b>710.9</b>	<b>754.4</b>	<b>710.9</b>	<b>754.4</b>
Fee and commission income	4(iv)	166.5	178.5	166.5	178.5
Fee and commission expense	4(v)	(62.3)	(61.1)	(62.3)	(61.1)
<b>Net fee and commission income</b>		<b>104.2</b>	<b>117.4</b>	<b>104.2</b>	<b>117.4</b>
Net trading income	4(vi)	95.1	107.9	95.1	107.9
Net loss from financial instruments designated at fair value	4(vii)	(1.6)	(1.5)	(1.6)	(1.5)
Net loss on derivatives measured at fair value through profit or loss		—	(0.2)	—	(0.2)
Net gain from disposal of financial assets measured at fair value through other comprehensive income	4(viii)	27.2	37.1	27.2	37.1
Other operating income	4(iii)	140.6	153.0	140.6	153.0
<b>Net other operating income</b>		<b>261.3</b>	<b>296.3</b>	<b>261.3</b>	<b>296.3</b>
Operating income before change in expected credit losses and other credit risk provisions		1,076.4	1,168.1	1,076.4	1,168.1
Net change in expected credit losses and other credit risk provisions	5	(46.2)	7.3	(46.2)	7.3
<b>Net operating income</b>		<b>1,030.2</b>	<b>1,175.4</b>	<b>1,030.2</b>	<b>1,175.4</b>
Operating expenses					
– employee compensation and benefits	6	(334.3)	(330.9)	(334.3)	(330.9)
– premises and equipment	6	(65.0)	(66.0)	(65.0)	(66.0)
– general and administrative expenses	6	(125.2)	(141.7)	(125.2)	(141.7)
– other expenses	6	(190.7)	(162.4)	(190.7)	(162.4)
<b>Total operating expenses</b>		<b>(715.2)</b>	<b>(701.0)</b>	<b>(715.2)</b>	<b>(701.0)</b>
<b>Profit before income tax</b>		<b>315.0</b>	<b>474.4</b>	<b>315.0</b>	<b>474.4</b>
Income tax expense	8	(94.7)	(144.0)	(94.7)	(144.0)
<b>Profit for the year</b>		<b>220.3</b>	<b>330.4</b>	<b>220.3</b>	<b>330.4</b>
<b>Attributable to equity holders of the parent</b>		<b>220.3</b>	<b>330.4</b>	<b>220.3</b>	<b>330.4</b>

The notes on pages 9 to 57 are an integral part of these consolidated financial statements.

### Statements of comprehensive income

for the year ended 31 December 2020

	Consolidated		Company	
	2020 \$m	2019 \$m	2020 \$m	2019 \$m
Profit for the year	220.3	330.4	220.3	330.4
<b>Other comprehensive income</b>				
<b>Items that may be reclassified to Income statements:</b>				
Financial assets measured at fair value through other comprehensive income				
– fair value gains recognised in other comprehensive income	62.8	46.7	62.8	46.7
– net amount transferred to Income statements	(27.2)	(37.0)	(27.2)	(37.0)
– deferred tax on items taken directly to or transferred from equity	(10.0)	(4.7)	(10.0)	(4.7)
– other movements	2.7	—	2.7	—
Cash flow hedges				
– effective portion of changes in fair value	0.4	3.0	0.4	3.0
– deferred tax on items taken directly to or transferred from equity	(0.1)	(0.9)	(0.1)	(0.9)
Changes in fair value of financial liabilities designated at fair value upon initial recognition arising from changes in own credit risk	(0.1)	(0.1)	(0.1)	(0.1)
Total other comprehensive income	28.5	7.0	28.5	7.0
<b>Total comprehensive income for the year</b>	<b>248.8</b>	<b>337.4</b>	<b>248.8</b>	<b>337.4</b>
<b>Attributable to equity holders of the parent</b>	<b>248.8</b>	<b>337.4</b>	<b>248.8</b>	<b>337.4</b>

The notes on pages 9 to 57 are an integral part of these consolidated financial statements.

## Statements of financial position

at 31 December 2020

	Notes	Consolidated		Company	
		2020	2019	2020	2019
		\$m	\$m	\$m	\$m
<b>Assets</b>					
Cash and balances at central banks		3,342.6	1,633.1	3,342.6	1,633.1
Items in the course of collection from other banks		1.9	5.9	1.9	5.9
Other financial assets mandatorily measured at fair value through profit or loss		4.4	4.2	4.4	4.2
Derivatives	9	178.7	74.5	178.7	74.5
Loans and advances to banks	27	14.9	25.5	14.9	25.5
Loans and advances to customers	27	30,232.2	29,260.7	30,232.2	29,260.7
Financial assets measured at fair value through other comprehensive income	10	12,060.7	11,483.8	12,060.7	11,483.8
Receivables from related entities	33	200.4	147.6	200.2	147.6
Other assets	14	568.9	488.1	573.6	485.3
Right-of-use assets	24	212.0	230.4	212.0	230.4
Property, plant and equipment	11	48.8	44.1	48.8	44.1
Net deferred tax assets	15	101.6	102.0	101.6	102.0
Intangible assets	13	69.2	73.1	69.2	73.1
<b>Total assets</b>		<b>47,036.3</b>	<b>43,573.0</b>	<b>47,040.8</b>	<b>43,570.2</b>
<b>Liabilities</b>					
Deposits by banks		587.1	930.9	587.1	930.9
Items in the course of transmission to other banks		45.1	60.2	45.1	60.2
Sale and repurchase agreements – non-trading		2,046.9	1,457.6	2,046.9	1,457.6
Financial liabilities designated at fair value	16	43.2	43.7	43.2	43.7
Derivatives	9	359.9	160.2	359.9	160.2
Customer accounts – amortised cost		36,524.4	32,455.3	36,524.4	32,455.3
Debt securities on issue	18	892.9	100.0	—	100.0
Provisions for liabilities and charges	17	21.7	16.4	21.7	16.4
Payables to related entities	33	3,180.0	5,307.3	4,073.5	5,307.3
Other liabilities	19	149.9	171.3	153.8	168.5
Lease liabilities	24	224.9	236.2	224.9	236.2
Employee benefits	20	95.9	90.5	95.9	90.5
<b>Total liabilities</b>		<b>44,171.9</b>	<b>41,029.6</b>	<b>44,176.4</b>	<b>41,026.8</b>
<b>Net assets</b>		<b>2,864.4</b>	<b>2,543.4</b>	<b>2,864.4</b>	<b>2,543.4</b>
<b>Equity</b>					
Share capital	21	811.0	811.0	811.0	811.0
Reserves	22	439.2	259.4	439.2	259.4
Retained earnings		1,614.2	1,473.0	1,614.2	1,473.0
<b>Total equity</b>		<b>2,864.4</b>	<b>2,543.4</b>	<b>2,864.4</b>	<b>2,543.4</b>

The notes on pages 9 to 57 are an integral part of these consolidated financial statements.

**Statement of changes in equity – consolidated**
**for the year ended 31 December 2020**

	Share capital \$m	Own credit spread reserve \$m	FVOCI reserve \$m	Cash flow hedging reserve \$m	Capital contribution reserve \$m	Other capital reserve \$m	Retained profits \$m	Total \$m
<b>At 1 Jan 2020</b>	<b>811.0</b>	<b>—</b>	<b>6.2</b>	<b>(0.4)</b>	<b>3.6</b>	<b>250.0</b>	<b>1,473.0</b>	<b>2,543.4</b>
Profit for the year	—	—	—	—	—	—	220.3	220.3
<b>Other comprehensive income (net of income tax)</b>								
Cash flow hedges								
– effective portion of changes in fair value	—	—	—	0.3	—	—	—	0.3
– net amount transferred to Income statement	—	—	—	—	—	—	—	—
Financial assets measured at fair value through other comprehensive income								
– net change in fair value	—	—	62.8	—	—	—	—	62.8
– net amount transferred to Income statement	—	—	(34.5)	—	—	—	—	(34.5)
Changes in fair value of financial liabilities designated at fair value upon initial recognition arising from changes in own credit risk	—	(0.9)	—	—	—	—	0.8	(0.1)
<b>Total other comprehensive income</b>	<b>—</b>	<b>(0.9)</b>	<b>28.3</b>	<b>0.3</b>	<b>—</b>	<b>—</b>	<b>0.8</b>	<b>28.5</b>
<b>Total comprehensive income for year</b>	<b>—</b>	<b>(0.9)</b>	<b>28.3</b>	<b>0.3</b>	<b>—</b>	<b>—</b>	<b>221.1</b>	<b>248.8</b>
<b>Transactions with owners, recorded directly in equity</b>								
Contributions by and distributions to owners								
Tier 1 issuance of capital	—	—	—	—	—	150.0	—	150.0
Share based payments	—	—	—	—	2.1	—	(0.3)	1.8
Dividends to equity holders	—	—	—	—	—	—	(79.6)	(79.6)
<b>Total contributions by and distributions to owners</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>2.1</b>	<b>150.0</b>	<b>(79.9)</b>	<b>72.2</b>
<b>At 31 Dec 2020</b>	<b>811.0</b>	<b>(0.9)</b>	<b>34.5</b>	<b>(0.1)</b>	<b>5.7</b>	<b>400.0</b>	<b>1,614.2</b>	<b>2,864.4</b>
At 1 Jan 2019	811.0	0.1	1.2	(2.5)	4.1	250.0	1,305.0	2,368.9
Profit for the year	—	—	—	—	—	—	330.4	330.4
Other comprehensive income (net of income tax)								
Cash flow hedges								
– effective portion of changes in fair value	—	—	—	2.1	—	—	—	2.1
– net amount transferred to Income statement	—	—	—	—	—	—	—	—
Financial assets measured at fair value through other comprehensive income								
– net change in fair value	—	—	46.7	—	—	—	—	46.7
– net amount transferred to Income statement	—	—	(41.7)	—	—	—	—	(41.7)
Changes in fair value of financial liabilities designated at fair value upon initial recognition arising from changes in own credit risk	—	(0.1)	—	—	—	—	—	(0.1)
<b>Total other comprehensive income</b>	<b>—</b>	<b>(0.1)</b>	<b>5.0</b>	<b>2.1</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>7.0</b>
<b>Total comprehensive income for year</b>	<b>—</b>	<b>(0.1)</b>	<b>5.0</b>	<b>2.1</b>	<b>—</b>	<b>—</b>	<b>330.4</b>	<b>337.4</b>
<b>Transactions with owners, recorded directly in equity</b>								
Contributions by and distributions to owners								
Share based payments	—	—	—	—	(0.5)	—	0.1	(0.4)
Dividends to equity holders	—	—	—	—	—	—	(162.5)	(162.5)
<b>Total contributions by and distributions to owners</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>(0.5)</b>	<b>—</b>	<b>(162.4)</b>	<b>(162.9)</b>
<b>At 31 Dec 2019</b>	<b>811.0</b>	<b>—</b>	<b>6.2</b>	<b>(0.4)</b>	<b>3.6</b>	<b>250.0</b>	<b>1,473.0</b>	<b>2,543.4</b>

The notes on pages 9 to 57 are an integral part of these consolidated financial statements.



## Statement of changes in equity – company

for the year ended 31 December 2020

	Share capital \$m	Own credit spread reserve \$m	FVOCI reserve \$m	Cash flow hedging reserve \$m	Capital contribution reserve \$m	Other capital reserve \$m	Retained profits \$m	Total \$m
<b>At 1 Jan 2020</b>	<b>811.0</b>	<b>—</b>	<b>6.2</b>	<b>(0.4)</b>	<b>3.6</b>	<b>250.0</b>	<b>1,473.0</b>	<b>2,543.4</b>
Profit for the year	—	—	—	—	—	—	220.3	220.3
<b>Other comprehensive income (net of income tax)</b>								
Cash flow hedges								
– effective portion of changes in fair value	—	—	—	0.3	—	—	—	0.3
– net amount transferred to Income statement	—	—	—	—	—	—	—	—
Financial assets measured at fair value through other comprehensive income								
– net change in fair value	—	—	62.8	—	—	—	—	62.8
– net amount transferred to Income statement	—	—	(34.5)	—	—	—	—	(34.5)
Changes in fair value of financial liabilities designated at fair value upon initial recognition arising from changes in own credit risk	—	(0.9)	—	—	—	—	0.8	(0.1)
<b>Total other comprehensive income</b>	<b>—</b>	<b>(0.9)</b>	<b>28.3</b>	<b>0.3</b>	<b>—</b>	<b>—</b>	<b>0.8</b>	<b>28.5</b>
<b>Total comprehensive income for year</b>	<b>—</b>	<b>(0.9)</b>	<b>28.3</b>	<b>0.3</b>	<b>—</b>	<b>—</b>	<b>221.1</b>	<b>248.8</b>
<b>Transactions with owners, recorded directly in equity</b>								
Contributions by and distributions to owners								
Tier 1 issuance of capital	—	—	—	—	—	150.0	—	150.0
Share based payments	—	—	—	—	2.1	—	(0.3)	1.8
Dividends to equity holders	—	—	—	—	—	—	(79.6)	(79.6)
<b>Total contributions by and distributions to owners</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>2.1</b>	<b>150.0</b>	<b>(79.9)</b>	<b>72.2</b>
<b>At 31 Dec 2020</b>	<b>811.0</b>	<b>(0.9)</b>	<b>34.5</b>	<b>(0.1)</b>	<b>5.7</b>	<b>400.0</b>	<b>1,614.2</b>	<b>2,864.4</b>
At 1 Jan 2019	811.0	0.1	1.2	(2.5)	4.1	250.0	1,305.0	2,368.9
Profit for the year	—	—	—	—	—	—	330.4	330.4
Other comprehensive income (net of income tax)								
Cash flow hedges								
– effective portion of changes in fair value	—	—	—	2.1	—	—	—	2.1
– net amount transferred to Income statement	—	—	—	—	—	—	—	—
Financial assets measured at fair value through other comprehensive income								
– net change in fair value	—	—	46.7	—	—	—	—	46.7
– net amount transferred to Income statement	—	—	(41.7)	—	—	—	—	(41.7)
Changes in fair value of financial liabilities designated at fair value upon initial recognition arising from changes in own credit risk	—	(0.1)	—	—	—	—	—	(0.1)
<b>Total other comprehensive income</b>	<b>—</b>	<b>(0.1)</b>	<b>5.0</b>	<b>2.1</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>7.0</b>
<b>Total comprehensive income for year</b>	<b>—</b>	<b>(0.1)</b>	<b>5.0</b>	<b>2.1</b>	<b>—</b>	<b>—</b>	<b>330.4</b>	<b>337.4</b>
<b>Transactions with owners, recorded directly in equity</b>								
Contributions by and distributions to owners								
Share based payments	—	—	—	—	(0.5)	—	0.1	(0.4)
Dividends to equity holders	—	—	—	—	—	—	(162.5)	(162.5)
<b>Total contributions by and distributions to owners</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>—</b>	<b>(0.5)</b>	<b>—</b>	<b>(162.4)</b>	<b>(162.9)</b>
<b>At 31 Dec 2019</b>	<b>811.0</b>	<b>—</b>	<b>6.2</b>	<b>(0.4)</b>	<b>3.6</b>	<b>250.0</b>	<b>1,473.0</b>	<b>2,543.4</b>

The notes on pages 9 to 57 are an integral part of these consolidated financial statements.

Statements of cash flows

for the year ended 31 December 2020

	Notes	Consolidated		Company	
		2020	2019	2020	2019
		\$m	\$m	\$m	\$m
<b>Cash flows from operating activities</b>					
Interest received		929.9	1,182.1	929.9	1,182.1
Interest paid		(211.0)	(442.7)	(211.0)	(442.7)
Other income received		344.5	378.9	337.9	379.1
Other expenses paid		(692.4)	(822.6)	(685.6)	(823.7)
Loans and bills advanced		(1,069.7)	(3,535.8)	(1,069.5)	(3,535.8)
Net increase/(decrease) in deposits, repo and other borrowings		2,116.6	5,829.8	3,010.1	5,829.8
Net (increase)/decrease in trading assets		95.5	105.4	95.5	105.4
Net (increase)/decrease from movements in other assets/liabilities		(101.7)	(7.3)	(102.7)	(6.4)
Income tax paid		(124.1)	(144.0)	(124.1)	(144.0)
<b>Net cash from operating activities</b>	29	1,287.6	2,543.8	2,180.5	2,543.8
<b>Cash flows from investing activities</b>					
Purchases of investment securities		(10,890.6)	(12,885.8)	(10,890.6)	(12,885.8)
Purchase of property, plant and equipment		(14.3)	(15.4)	(14.3)	(15.4)
Payments for intangible assets		(1.4)	(6.1)	(1.4)	(6.1)
Proceeds from sale and maturity of investments		10,386.9	10,756.0	10,386.9	10,756.0
<b>Net cash (used in) investing activities</b>		(519.4)	(2,151.3)	(519.4)	(2,151.3)
<b>Cash flows from financing activities</b>					
Issuance of debt securities		1,000.0	—	—	—
Redemption of debt securities		(207.6)	(333.1)	(100.5)	(333.1)
Proceeds of subordinated debt issue		100.0	—	100.0	—
Further issuance of Tier 1 Capital		150.0	—	150.0	—
Dividends paid		(79.6)	(162.5)	(79.6)	(162.5)
Principal elements of finance lease payments		(32.1)	(33.8)	(32.1)	(33.8)
<b>Net cash (used in) / provided by financing activities</b>		930.7	(529.4)	37.8	37.8
Net increase/(decrease) in cash and cash equivalents held		1,698.9	(136.9)	1,698.9	(136.9)
<b>Cash and cash equivalents at the beginning of the year</b>		1,658.6	1,795.5	1,658.6	1,795.5
<b>Cash and cash equivalents at the end of the year</b>	29	3,357.5	1,658.6	3,357.5	1,658.6

The notes on pages 9 to 57 are an integral part of these consolidated financial statements.

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# Notes on the Consolidated financial statements

## 1 Reporting entity

HSBC Bank Australia Limited is a company domiciled in Australia. The consolidated financial report of the Company for the year ended 31 December 2020 comprises the 'Company' or the 'Bank' and its subsidiaries (together referred to as the 'consolidated entity'). References to 'HSBC' or 'the HSBC Group' within this document mean HSBC Holdings plc together with its subsidiaries. The consolidated entity operates as a profit entity.

## 2 Basis of preparation

### (a) Statement of compliance

The financial report is a general purpose financial report which has been prepared in accordance with Australian Accounting Standards ('AASBs'), including Australian interpretations, adopted by the Australian Accounting Standards Board and the Corporations Act 2001. The consolidated financial report of the consolidated entity and the financial report of the Company comply with International Financial Reporting Standards ('IFRS') and interpretations adopted by the International Accounting Standards Board.

The financial report was authorised for issue by the Board of Directors on 15 February 2021.

### (b) Basis of measurement

The financial report is prepared on the historical cost basis except that the following assets and liabilities are stated at their fair value: derivative financial instruments, trading assets/liabilities, assets and liabilities designated at fair value and financial instruments classified as fair value through other comprehensive income ('FVOCI'). The methods used to measure fair values are discussed further in note 28.

### (c) Functional and presentational currency

The financial report is presented in Australian dollars, which is the Bank's functional and presentation currency.

The Company is of the kind referred to in ASIC Legislative Instrument 2016/191, relating to the 'rounding off' of amounts in the financial statements. Amounts in the financial statements have been rounded, where appropriate, to the nearest tenth of a million dollars except where otherwise stated.

### (d) Going concern

These financial statements are prepared on a going concern basis, as the directors are satisfied that the Bank has the resources to continue in business for the foreseeable future. In making this assessment, the directors have considered a wide range of information relating to present and future conditions, including future projections of profitability, cash flows, capital requirements and capital resources. These considerations include stressed scenarios that reflect the increasing uncertainty that the global pandemic has had on the bank's operations, as well as considering potential impacts from other top and emerging risks, and the related impact on profitability, capital and liquidity.

### (e) Critical accounting estimates and judgements in applying accounting policies

The preparation of a financial report in conformity with AASBs requires management to make judgements, estimates and assumptions that affect the application of accounting policies and reported amounts of assets and liabilities, income and expenses. Use of available information and application of judgement are inherent in the formation of estimates. Actual results in the future may differ from those reported.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

The accounting policies that are deemed critical to the results and financial position, in terms of the materiality of the items to which the policies are applied and the high degree of judgement involved, including the use of assumptions and estimation, are discussed below.

#### Loan impairment

In determining Expected Credit Loss ('ECL'), management is required to exercise judgement in defining what is considered to be a significant increase in credit risk and in making assumptions and estimates to incorporate relevant information about past events, current conditions and forecasts of economic conditions. Judgement has been applied in determining the lifetime and point of initial recognition of revolving facilities. The probability of default ('PD'), loss given default ('LGD') and exposure at default ('EAD') models, which support these determinations are reviewed regularly in light of differences between loss estimates and actual loss experience.

The exercise of judgement in making estimations requires the use of assumptions which are highly subjective and very sensitive to the risk factors, in particular to changes in economic and credit conditions across a large number of geographical areas. Many of the factors have a high degree of interdependency and there is no single factor to which loan impairment allowances as a whole are sensitive. Note 27 outlines the assumptions underlying the Central scenario and information about how scenarios are developed in relation to the HSBC Group's top and emerging risks and its judgements, informed by consensus forecasts of professional industry forecasters. The sensitivity of ECL to different economic scenarios is illustrated by recalculating the ECL for selected portfolios as if 100% weighting had been assigned to each scenario.

Application of the Bank's methodology for loan impairment is set out in Statement of significant accounting policies note 3. However, for stage 3 impaired loans, judgement is required in determining, first, whether there are indications that an impairment loss may have already been incurred, and then estimating the amount and timing of expected cash flows, which form the basis of the impairment loss that is recorded.

#### Valuation of financial instruments

The consolidated entity's accounting policy for valuation of financial instruments is included in note 3(k) 'Sale and repurchase agreements' and is discussed further within note 9 'Derivatives' and note 28 'Fair values of financial instruments carried at fair value'.

## Notes on the Consolidated Financial Statements

The best evidence of fair value is a quoted price in an actively traded principal market. The fair values of financial instruments that are quoted in active markets are based on bid prices for assets held and offer prices for liabilities issued. Where a financial instrument has a quoted price in an active market, the fair value of the total holding of the financial instrument is calculated as the product of the number of units and quoted price. The judgement as to whether a market is active may include, but is not restricted to, the consideration of factors such as the magnitude and frequency of trading activity, the availability of prices and the size of bid/offer spreads. The bid/offer spread represents the difference in prices at which a market participant would be willing to buy compared with the price at which they would be willing to sell. Valuation techniques may incorporate assumptions about factors that other market participants would use in their valuations, including:

- the likelihood and expected timing of future cash flows on the instrument. These cash flows are usually governed by the terms of the instrument, although management judgement may be required when the ability of the counterparty to service the instrument in accordance with the contractual terms is in doubt;
- an appropriate discount rate for the instrument. Management determines this rate based on its assessment of the appropriate spread of the rate for the instrument over the risk-free rate; and
- judgement to determine what model to use to calculate fair value in areas where the choice of valuation model is particularly subjective, for example, when valuing complex derivative models.

A range of valuation techniques are employed, dependent on the instrument type and available market data. Most valuation techniques are based upon discounted cash flow analyses, in which expected future cash flows are calculated and discounted to present value using a discounting curve. Prior to considering credit risk, the expected future cash flows may be known, as would be the case for the fixed leg of an interest rate swap, or may be uncertain and require projection, as would be the case for the floating leg of an interest rate swap. 'Projection' utilises market forward curves, if available. In option models, the probability of different potential future outcomes must be considered. In addition, the value of some products is dependent on more than one market factor, and in these cases it will typically be necessary to consider how movements in one market factor may affect the other market factors. The model inputs necessary to perform such calculations include interest rate yield curves, exchange rates, volatilities, correlations, prepayments and default rates. For interest rate derivatives with collateralised counterparties and in significant currencies, the Bank uses a discounting curve that reflects the overnight interest rate.

The majority of valuation techniques employ only observable market data. However, certain financial instruments are valued on the basis of valuation techniques that feature one or more significant market inputs that are unobservable, and for them the measurement of fair value is more judgemental. An instrument in its entirety is classified as valued using significant unobservable inputs if, in the opinion of management, a significant proportion of the instrument's inception profit or greater than 5% of the instrument's valuation is driven by unobservable inputs. 'Unobservable' in this context means that there is little or no current market data available from which to determine the price at which an arm's length transaction would be likely to occur. It generally does not mean that there is no data available at all upon which to base a determination of fair value (consensus pricing data may, for example, be used).

### Provision for liabilities and charges

The Consolidated entity assesses whether it is probable that an outflow of economic benefits will be required to settle a current legal or constructive obligation as a result of past events. These calculations involve an estimation of the potential loss and likelihood of that loss and details of these can be found in note 17.

### Goodwill impairment

The review of goodwill for impairment reflects management's best estimate of the future cash flows of the cash-generating units ('CGUs') and the rates used to discount these cash flows, both of which are subject to uncertain factors as follows:

- the future cash flows of the CGUs are sensitive to the cash flows projected for the periods for which detailed forecasts are available and to assumptions regarding the long-term pattern of sustainable cash flows thereafter. Forecasts are compared with actual performance and verifiable economic data, but they reflect management's view of future business prospects at the time of the assessment; and
- the rates used to discount future expected cash flows can have a significant effect on their valuation and are based on the costs of capital assigned to individual CGUs. These variables are subject to fluctuations in external market rates and economic conditions beyond management's control and are subject to uncertainty requiring the exercise of significant judgement.

The accuracy of forecast cash flows is subject to a high degree of uncertainty in volatile market conditions. In such circumstances, management retests goodwill for impairment more frequently than once a year when indicators of impairment exist to ensure that the assumptions on which the cash flow forecasts are based continue to reflect current market conditions and management's best estimate of future business prospects and these can be found in note 13.

### (f) Changes in accounting policies

There is only one new accounting standard adopted during 2020, which affects the financial statements.

#### AASB 2020-3 Interest Rate Benchmark Reform

AASB 2020-3 Australian Accounting Standards – Interest Rate Benchmark Reforms: Amendments to IFRS 9, IAS 39, IFRS 7, IFRS 4 and IFRS 16 issued in August 2020 represents the second phase of the IASB's project on the effects of interest rate benchmark reform, addressing issues affecting financial statements when changes are made to contractual cash flows and hedging relationships as a result of the reform.

Under these amendments, changes made to a financial instrument that are economically equivalent and required by interest rate benchmark reform do not result in the derecognition or a change in the carrying amount of the financial instrument, but instead require the effective interest rate to be updated to reflect the change in the interest rate benchmark. In addition, hedge accounting will not be discontinued solely because of the replacement of the interest rate benchmark if the hedge meets other hedge accounting criteria. These amendments apply from 1 January 2021 with early adoption permitted. The bank has adopted the amendments from 1 January 2020 and has made the additional disclosures as required by the amendments. Further information is included in note 35.

## **(g) Future accounting developments**

### **Minor developments to accounting standards**

The AASB has not published any minor amendments effective from 1 January 2021 that are applicable to the Bank. However, the AASB has published a number of minor amendments to IFRSs that are effective from 1 January 2022 and 1 January 2023. The Bank expects they will have an insignificant effect, when adopted, on the consolidated financial statements of the Bank.

## **3 Statement of significant accounting policies**

The accounting policies set out below have been applied consistently to all periods presented in the consolidated financial statements. Certain comparative amounts have been reclassified to conform with the current year presentation.

### **(a) Principles of consolidation**

#### **Subsidiaries**

Subsidiaries are entities controlled by the Company. The Company controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity.

Investments in subsidiaries are carried at their cost of acquisition, less provision for impairment, in the Company's financial statements.

#### **Special purpose entities**

Special purpose entities are entities that are created to accomplish a narrow and well-defined objective such as the securitisation of particular assets, or the execution of specific borrowing or lending transactions. The financial statements of special purpose entities are included in the consolidated entity's financial statements where the substance of the relationship is that the consolidated entity controls the special purpose entity.

#### **Transactions eliminated on consolidation**

Intragroup balances and any unrealised gains and losses or income and expenses arising from intragroup transactions, are eliminated in preparing the consolidated financial statements. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

### **(b) Foreign currency transactions**

Items included in each of the entities of the consolidated entity are measured using the currency of the primary economic environment in which the entity operates (the 'functional currency'). The consolidated entity's financial statements are presented in Australian dollars which is the Bank's functional and presentation currency.

Transactions in foreign currencies are translated at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to Australian dollars at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the Income statement. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to Australian dollars at foreign exchange rates ruling at the dates the fair value was determined.

### **(c) Interest income and expense**

Interest income and expense for all financial instruments, excluding those classified as held for trading or designated at fair value are recognised in 'Interest income' and 'Interest expense' in the Income statement using the effective interest rate method. However, as an exception to this, interest on debt securities issued by the Bank that are designated under the fair value option and derivatives managed in conjunction with those debt securities are included in interest expense. Interest on impaired financial assets is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

### **(d) Non-interest income**

#### **Fee income**

The Bank generates fee income from services provided at a fixed price over time, such as account service and card fees, or when the Bank delivers a specific transaction at a point in time such as broking services and import/export services. With the exception of certain fund management and performance fees, all other fees are generated at a fixed price. Fund management and performance fees can be variable depending on the size of the customer portfolio and HSBC's performance as fund manager. Variable fees are recognised when all uncertainties are resolved. Fee income is generally earned from short-term contracts with payment terms that do not include a significant financing component.

The Bank acts as principal in the majority of contracts with customers, with the exception of broking services. For most brokerage trades, the Bank acts as agent in the transaction and recognises broking income net of fees payable to other parties in the arrangement.

The Bank recognises fees earned on transaction-based arrangements at a point in time when we have fully provided the service to the customer. Where the contract requires services to be provided over time, income is recognised on a systematic basis over the life of the agreement. Where the Bank offers a package of services that contains multiple non-distinct performance obligations, such as those included in account service packages, the promised services are treated as a single performance obligation. If a package of services contains distinct performance obligations, such as those including both account and insurance services, the corresponding transaction price is allocated to each performance obligation based on the estimated stand-alone selling prices.

#### **Net income/(expense) from financial instruments measured at fair value through profit or loss**

Net income/(expense) from financial instruments measured at fair value through profit or loss includes the following:

- 'Net income from financial instruments held for trading or managed on a fair value basis': This is comprised of the net trading income, which includes all gains and losses from changes in the fair value of financial assets and financial liabilities held for trading, together with the related interest income, expense and dividends; and it also includes all gains and losses from changes in the fair value of derivatives that are managed in conjunction with financial assets and liabilities measured at fair value through profit or loss.

## Notes on the Consolidated Financial Statements

- 'Dividend income' is recognised when the right to receive payment is established. This is the ex-dividend date for listed equity securities, and usually the date when shareholders approve the dividend for unlisted equity securities.
- 'Changes in fair value of long-term debt and related derivatives': Interest paid on the external long-term debt and interest cash flows on related derivatives is presented in interest expense.
- 'Changes in fair value of other financial instruments mandatorily measured at fair value through profit or loss': This includes interest on instruments which fail the solely payments of principal and interest ('SPPI') test.

### Net income from financial instruments designated at fair value

Net income from financial instruments designated at fair value comprises all gains and losses from changes in the fair value of such financial assets and financial liabilities, together with interest income and expense and dividend income attributable to those financial instruments. Interest income and expense and dividend income arising on these financial instruments are also included, except for interest arising from debt securities issued, and derivatives managed in conjunction which was with those debt securities, which is recognised in 'Interest expense' note 4(ii).

### (e) Financial instruments measured at amortised cost

Financial assets that are held to collect the contractual cash flows and that contain contractual terms that give rise on specified dates to cash flows that are solely payments of principal and interest, such as most loans and advances to banks and customers and some debt securities, are measured at amortised cost. In addition, most financial liabilities are measured at amortised cost. The Bank accounts for regular-way amortised cost financial instruments using trade date accounting. The carrying value of these financial assets at initial recognition includes any directly attributable transaction costs. If the initial fair value is lower than the cash amount advanced, such as in the case of some leveraged finance and syndicated lending activities, the difference is deferred and recognised over the life of the loan through the recognition of interest income.

### Non-trading reverse repurchase, repurchase and similar agreements

When debt securities are sold subject to a commitment to repurchase them at a predetermined price ('repos'), they remain on the balance sheet and a liability is recorded in respect of the consideration received. Securities purchased under commitments to resell ('reverse repos') are not recognised on the balance sheet and an asset is recorded in respect of the initial consideration paid. Non-trading repos and reverse repos are measured at amortised cost. The difference between the sale and repurchase price or between the purchase and resale price is treated as interest and recognised in net interest income over the life of the agreement.

Contracts that are economically equivalent to reverse repurchase or repurchase agreements (such as sales or purchases of debt securities entered into together with total return swaps with the same counterparty) are accounted for similarly to, and presented together with, reverse repurchase or repurchase agreements.

### (f) Impairment of amortised cost and FVOCI financial assets

Expected credit losses ('ECL') are recognised for loans and advances to banks and customers, non-trading reverse repurchase agreements, other financial assets held at amortised cost, debt instruments measured at FVOCI, and certain loan commitments and financial guarantee contracts. At initial recognition, allowance (or provision in the case of some loan commitments and financial guarantees) is required for ECL resulting from default events that are possible within the next 12 months (or less, where the remaining life is less than 12 months) ('12-month ECL'). In the event of a significant increase in credit risk, allowance (or provision) is required for ECL resulting from all possible default events over the expected life of the financial instrument ('lifetime ECL'). Financial assets where 12-month ECL is recognised are considered to be 'stage 1'; financial assets which are considered to have experienced a significant increase in credit risk are in 'stage 2'; and financial assets for which there is objective evidence of impairment so are considered to be in default or otherwise credit impaired are in 'stage 3'. Purchased or originated credit impaired financial assets ('POCI') are treated differently as set out below.

### Credit impaired (stage 3)

The Bank determines that a financial instrument is credit impaired and in stage 3 by considering relevant objective evidence, primarily whether:

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

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

### Write-off

Financial assets (and the related impairment allowances) are normally written off, either partially or in full, when there is no realistic prospect of recovery. Where loans are secured, this is generally after receipt of any proceeds from the realisation of security. In circumstances where the net realisable value of any collateral has been determined and there is no reasonable expectation of further recovery, write-off may be earlier.

### Renegotiation

Loans are identified as renegotiated and classified as credit impaired when the Bank modifies the contractual payment terms due to significant credit distress of the borrower. Renegotiated loans remain classified as credit impaired until there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows and retain the designation of renegotiated until maturity or derecognition.

A loan that is renegotiated is derecognised if the existing agreement is cancelled and a new agreement is made on substantially different terms or if the terms of an existing agreement are modified such that the renegotiated loan is a substantially different financial instrument. Any new loans that arise following derecognition events in these circumstances are considered to be POCI and will continue to be disclosed as renegotiated loans.



Other than originated credit-impaired loans, all other modified loans could be transferred out of stage 3 if they no longer exhibit any evidence of being credit impaired and, in the case of renegotiated loans, there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows, over the minimum observation period, and there are no other indicators of impairment. These loans could be transferred to stage 1 or 2 based on the mechanism as described below by comparing the risk of a default occurring at the reporting date (based on the modified contractual terms) and the risk of a default occurring at initial recognition (based on the original, unmodified contractual terms). Any amount written off as a result of the modification of contractual terms would not be reversed.

### Loan modifications that are not credit impaired

Loan modifications that are not identified as renegotiated are considered to be commercial restructuring. Where a commercial restructuring results in a modification (whether legalised through an amendment to the existing terms or the issuance of a new loan contract) such that Bank's rights to the cash flows under the original contract have expired, the old loan is derecognised and the new loan is recognised at fair value. The rights to cash flows are generally considered to have expired if the commercial restructure is at market rates and no payment-related concession has been provided.

### Significant increase in credit risk (stage 2)

An assessment of whether credit risk has increased significantly since initial recognition is performed at each reporting period by considering the change in the risk of default occurring over the remaining life of the financial instrument. The assessment explicitly or implicitly compares the risk of default occurring at the reporting date compared with that at initial recognition, taking into account reasonable and supportable information, including information about past events, current conditions and future economic conditions. The assessment is unbiased, probability-weighted, and to the extent relevant, uses forward-looking information consistent with that used in the measurement of ECL. The analysis of credit risk is multifactor. The determination of whether a specific factor is relevant and its weight compared with other factors depends on the type of product, the characteristics of the financial instrument and the borrower, and the geographical region. Therefore, it is not possible to provide a single set of criteria that will determine what is considered to be a significant increase in credit risk and these criteria will differ for different types of lending, particularly between retail and wholesale. However, unless identified at an earlier stage, all financial assets are deemed to have suffered a significant increase in credit risk when 30 days past due. In addition, wholesale loans that are individually assessed, typically corporate and commercial customers, and included on a watch or worry list, are included in stage 2.

For wholesale portfolios, the quantitative comparison assesses default risk using a lifetime probability of default which encompasses a wide range of information including the obligor's customer risk rating ('CRR'), macroeconomic condition forecasts and credit transition probabilities. Significant increase in credit risk is measured by comparing the average probability of default ('PD') for the remaining term estimated at origination with the equivalent estimation at reporting date. For origination CRRs up to 3.3, a significant increase in credit risk is considered to have occurred when the PD increase exceeds the below thresholds. For CRRs greater than 3.3 which are not impaired, a significant increase in credit risk is considered to have occurred when the origination PD has doubled. The significance of changes in PD was informed by expert credit risk judgement, referenced to historical credit migrations and to relative changes in external market rates. The quantitative measure of significance varies depending on the credit quality at origination as follows:

Origination CRR	Significance trigger – PD to increase by
0.1–1.2	15bps
2.1–3.3	30 bps
Greater than 3.3 and not impaired	2x

For loans originated prior to the implementation of IFRS 9, the origination PD does not include adjustments to reflect expectations of future macroeconomic conditions since these are not available without the use of hindsight. In the absence of this data, origination PD must be approximated assuming through-the-cycle PDs and migration probabilities, consistent with the instrument's underlying modelling approach and the CRR at origination. For these loans, the quantitative comparison is supplemented with additional CRR deterioration-based thresholds as set out in the table below:

Origination CRR	Additional significance criteria – Number of CRR grade notches deterioration required to identify as significant credit deterioration (stage 2) (> or equal to)
0.1	5 notches
1.1–4.2	4 notches
4.3–5.1	3 notches
5.2–7.1	2 notches
7.2–8.2	1 notch
8.3	0 notches

For certain portfolios of debt securities where external market ratings are available and credit ratings are not used in credit risk management, the debt securities will be in stage 2 if their credit risk increases to the extent they are no longer considered investment grade. Investment grade is where the financial instrument has a low risk of incurring losses, the structure has a strong capacity to meet its contractual cash flow obligations in the near term and adverse changes in economic and business conditions in the longer term may, but will not necessarily, reduce the ability of the borrower to fulfil their contractual cash flow obligations.

For retail portfolios, default risk is assessed using a reporting date 12-month PD derived from credit scores which incorporate all available information about the customer. This PD is adjusted for the effect of macroeconomic forecasts for periods longer than 12 months and is considered to be a reasonable approximation of a lifetime PD measure. Retail exposures are first segmented into homogeneous portfolios, generally by product and brand. Within each portfolio, the stage 2 accounts are defined as accounts with an adjusted 12-month PD greater than the average 12-month PD of loans in that portfolio 12 months before they become 30 days past due. The expert credit risk judgement is that no prior increase in credit risk is significant. This portfolio-specific threshold identifies loans with a PD higher than would be expected from loans that are performing as originally expected and higher than what would have been acceptable at origination. It therefore approximates a comparison of origination to reporting date PDs.

## Notes on the Consolidated Financial Statements

### Unimpaired and without significant increase in credit risk (stage 1)

ECL resulting from default events that are possible within the next 12 months are recognised for financial instruments that remain in stage 1.

### Movement between stages

Financial assets can be transferred between the different categories (other than 'POCI') depending on their relative increase in credit risk since initial recognition. Financial instruments are transferred out of stage 2 if their credit risk is no longer considered to be significantly increased since initial recognition based on the assessments described above. Except for renegotiated loans, financial instruments are transferred out of stage 3 when they no longer exhibit any evidence of credit impairment as described above. Renegotiated loans that are not POCI will continue to be in stage 3 until there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows, observed over a minimum one-year period and there are no other indicators of impairment. For loans that are assessed for impairment on a portfolio basis, the evidence typically comprises a history of payment performance against the original or revised terms, as appropriate to the circumstances. For loans that are assessed for impairment on an individual basis, all available evidence is assessed on a case-by-case basis.

### Measurement of ECL

The assessment of credit risk, and the estimation of ECL, are unbiased and probability-weighted, and incorporate all available information that is relevant to the assessment including information about past events, current conditions and reasonable and supportable forecasts of future events and economic conditions at the reporting date. In addition, the estimation of ECL should take into account the time value of money.

In general, the Bank calculates ECL using three main components, a PD, a loss given default ('LGD') and the exposure at default ('EAD').

The 12-month ECL is calculated by multiplying the 12-month PD, LGD and EAD. Lifetime ECL is calculated using the lifetime PD instead. The 12-month and lifetime PDs represent the probability of default occurring over the next 12 months and the remaining maturity of the instrument respectively.

The EAD represents the expected balance at default, taking into account the repayment of principal and interest from the balance sheet date to the default event together with any expected drawdowns of committed facilities. The LGD represents expected losses on the EAD given the event of default, taking into account, among other attributes, the mitigating effect of collateral value at the time it is expected to be realised and the time value of money.

The Bank leverages the Basel II internal ratings based ('IRB') framework where possible, with recalibration to meet the differing AASB 9 requirements set out in the table below:

Model	Regulatory capital	AASB 9
PD	<ul style="list-style-type: none"><li>Through the cycle (represents long-run average PD throughout a full economic cycle)</li><li>The definition of default includes a backstop of 90+ days past due</li></ul>	<ul style="list-style-type: none"><li>Point in time (based on current conditions, adjusted to take into account estimates of future conditions that will impact PD)</li><li>Default backstop of 90+ days past due for all portfolios</li></ul>
EAD	<ul style="list-style-type: none"><li>Cannot be lower than current balance</li></ul>	<ul style="list-style-type: none"><li>Amortisation captured for term products</li></ul>
LGD	<ul style="list-style-type: none"><li>Downturn LGD (consistent losses expected to be suffered during a severe but plausible economic downturn)</li><li>Regulatory floors may apply to mitigate risk of underestimating downturn LGD due to lack of historical data</li><li>Discounted using cost of capital</li><li>All collection costs included</li></ul>	<ul style="list-style-type: none"><li>Expected LGD (based on estimate of loss given default including the expected impact of future economic conditions such as changes in value of collateral)</li><li>No floors</li><li>Discounted using the original effective interest rate of the loan</li><li>Only costs associated with obtaining/selling collateral included</li></ul>
Other		<ul style="list-style-type: none"><li>Discounted back from point of default to balance sheet date</li></ul>

While 12-month PDs are recalibrated from Basel II models where possible, the lifetime PDs are determined by projecting the 12-month PD using a term structure. For the wholesale methodology, the lifetime PD also takes into account credit migration, i.e. a customer migrating through the CRR bands over its life.

The ECL for wholesale stage 3 is determined on an individual basis using a discounted cash flow methodology. The expected future cash flows are based on the credit risk officer's judgement as at the reporting date, reflecting reasonable and supportable assumptions and projections of future recoveries and expected future receipts of interest. Collateral is taken into account if it is likely that the recovery of the outstanding amount will include realisation of collateral based on its estimated fair value of collateral at the time of expected realisation, less costs for obtaining and selling the collateral. The cash flows are discounted at a reasonable approximation of the original effective interest rate. For significant cases, cash flows under four different scenarios are probability-weighted by reference to the three economic scenarios applied more generally by the Group and the judgement of the credit risk officer in relation to the likelihood of the workout strategy succeeding or receivership being required. For less significant cases, the effect of different economic scenarios and work-out strategies is approximated and applied as an adjustment to the most likely outcome.

### Period over which ECL is measured

ECL is measured from the initial recognition of the financial asset. The maximum period considered when measuring ECL (be it 12-month or lifetime ECL) is the maximum contractual period over which the Bank is exposed to credit risk. For wholesale overdrafts, credit risk management actions are taken no less frequently than on an annual basis and therefore this period is to the expected date of the next substantive credit review. The date of the substantive credit review also represents the initial recognition of the new facility. However, where the financial instrument includes both a drawn and undrawn commitment and the contractual ability to demand repayment and cancel the undrawn commitment does not serve to limit Bank's exposure to credit risk to the contractual notice period, the contractual period does not determine the maximum period considered. Instead, ECL is measured over the period the Bank remains exposed to credit risk that is not mitigated by credit risk management actions. This applies to retail overdrafts and credit cards, where the period is the average time taken for stage 2 exposures to default or close as performing accounts, determined on a portfolio basis and ranging from between two and six years. In addition, for these facilities it is not possible to identify the ECL on the loan commitment component separately from the financial asset component. As a result, the total ECL is recognised in the loss allowance for the financial asset unless the total ECL exceeds the gross carrying amount of the financial asset, in which case the ECL is recognised as a provision.



## Forward-looking economic inputs

The Bank will in general apply three forward-looking global economic scenarios determined with reference to external forecast distributions, the consensus economic scenario approach. This approach is considered sufficient to calculate unbiased expected loss in most economic environments. In certain economic environments, additional analysis may be necessary and may result in additional scenarios or adjustments, to reflect a range of possible economic outcomes sufficient for an unbiased estimate. The detailed methodology is disclosed in 'Measurement uncertainty and sensitivity analysis of ECL estimates in note 27.

### (g) Trading assets and trading liabilities

Treasury bills, customer accounts, loans and advances to and from banks, debt securities, structured deposits, equity shares, own debt issued and short positions in securities which have been acquired or incurred principally for the purpose of selling or repurchasing in the near term, or are part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking, are classified as held for trading. Financial assets and financial liabilities are recognised on trade date, when the Bank enters into contractual arrangements with counterparties to purchase or sell the financial instruments, and are normally derecognised when either sold (assets) or extinguished (liabilities). Measurement is initially at fair value, with transaction costs taken to the Income statement. Subsequently, the fair values are remeasured and gains and losses from changes therein are recognised in the Income statement within 'Net trading income'.

### (h) Financial instruments designated at fair value through profit or loss

Financial instruments, other than those held for trading, are classified in this category if they meet one or more of the criteria set out below and are so designated irrevocably at inception:

- the use of the designation removes or significantly reduces an accounting mismatch;
- a group of financial assets and liabilities or a group of financial liabilities is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy; and
- the financial liability contains one or more non-closely related embedded derivatives.

Designated financial assets are recognised when the Bank enters into contracts with counterparties, which is generally on trade date, and are normally derecognised when the rights to the cash flows expire or are transferred. Designated financial liabilities are recognised when the Bank enters into contracts with counterparties, which is generally on settlement date, and are normally derecognised when extinguished. Subsequent changes in fair values are recognised in the Income statement in 'Net income from financial instruments held for trading or managed on a fair value basis' or 'Net income/(expense) from assets and liabilities, including related derivatives, measured at fair value through profit or loss' except for the effect of changes in the liabilities' credit risk, which is presented in 'Other comprehensive income', unless that treatment would create or enlarge an accounting mismatch in profit or loss.

Under the above criterion, the main classes of financial instruments designated by the Bank are:

- Debt instruments for funding purposes that are designated to reduce an accounting mismatch: The interest and/or foreign exchange exposure on certain fixed-rate debt securities issued has been matched with the interest and/or foreign exchange exposure on certain swaps as part of a documented risk management strategy.
- Financial liabilities which contain both deposit and derivative components: These financial liabilities are managed and their performance evaluated on a fair value basis.

### (i) Financial assets measured at fair value through other comprehensive income ('FVOCI')

Financial assets held for a business model that is achieved by both collecting and selling contractual cash flows that contain contractual terms that give rise on specified dates to cash flows that are solely payments of principal and interest are measured at FVOCI. These comprise primarily debt securities. They are recognised on the trade date when the Bank enters into contractual arrangements to purchase and are normally derecognised when they are either sold or redeemed. They are subsequently remeasured at fair value and changes therein (except for those relating to impairment, interest income and foreign currency exchange gains and losses) are recognised in other comprehensive income until the assets are sold. Upon disposal, the cumulative gains or losses in other comprehensive income are recognised in the Income statement as 'Gains less losses from financial instruments'. Financial assets measured at FVOCI are included in the impairment calculations set out above and impairment is recognised in profit or loss.

### (j) Valuation of financial instruments

All financial instruments are initially recognised at fair value. Fair value is the price that would be received to sell an asset or be paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value of a financial instrument on initial recognition is generally its transaction price (that is, the fair value of the consideration given or received). However, if there is a difference between the transaction price and the fair value of financial instruments whose fair value is based on a quoted price in an active market or a valuation technique that uses only data from observable markets, the Bank recognises the difference as a trading gain or loss at inception ('day 1 gain or loss'). In all other cases, the entire day 1 gain or loss is deferred and recognised in the Income statement over the life of the transaction until the transaction matures or is closed out, the valuation inputs become observable or the Bank enters into an offsetting transaction. The fair value of financial instruments is generally measured on an individual basis. However, in cases where the Bank manages a group of financial assets and liabilities according to its net market or credit risk exposure, the fair value of the group of financial instruments is measured on a net basis but the underlying financial assets and liabilities are presented separately in the financial statements, unless they satisfy the offsetting criteria in note 3(n).

Subsequent to initial recognition, the fair values of financial instruments measured at fair value are measured in accordance with the Bank's valuation methodologies, which are described in note 28.

### (k) Sale and repurchase agreements

Where securities are sold subject to a commitment to repurchase them at a predetermined price ('repos'), they remain on the Statement of financial position and a liability is recorded in respect of the consideration received. Securities purchased under commitments to re-sell ('reverse repos') are not recognised on the Statement of financial position and the consideration paid is recorded in 'Advances to customers' or 'Advances with banks' as appropriate. The difference between the sale and repurchase price is treated as interest income and recognised over the life of the agreement.

## Notes on the Consolidated Financial Statements

Securities lending and borrowing transactions are generally secured, with collateral taking the form of securities or cash advanced or received. The transfer of securities to counterparties under these agreements is not normally reflected on the Statement of financial position. Cash collateral advanced or received is recorded as an asset or a liability respectively.

Securities borrowed are not recognised on the Statement of financial position. If they are sold on to third parties, an obligation to return the securities is recorded as a trading liability and measured at fair value, and any gains or losses are included in 'Net trading income'.

### (l) Derivatives and hedge accounting

#### Derivatives

Derivatives are recognised initially, and are subsequently remeasured, at fair value. Fair values of exchange-traded derivatives are obtained from quoted market prices. Fair values of over-the-counter derivatives are obtained using valuation techniques, including discounted cash flow models and option pricing models.

Derivatives are classified as assets when their fair value is positive, or as liabilities when their fair value is negative. Derivative assets and liabilities arising from different transactions are only offset if the transactions are with the same counterparty, a legal right of offset exists, and the parties intend to settle the cash flows on a net basis.

Gains and losses from changes in the fair value of derivatives, including the contractual interest, that do not qualify for hedge accounting are reported in 'Net trading income' except for derivatives managed in conjunction with financial instruments designated at fair value, where gains and losses are reported in 'Net income from financial instruments designated at fair value' together with the gains and losses on the economically hedged items. Where the derivatives are managed with debt securities on issue, the contractual interest is shown in 'Interest expense' together with the interest payable on the issued debt.

When derivatives are designated as hedges, the Bank classifies them as either:

- hedges of the change in fair value of recognised assets or liabilities or firm commitments ('fair value hedges'); or
- hedges of the variability in highly probable future cash flows attributable to a recognised asset or liability, or a forecast transaction ('cash flow hedges').

#### Hedge accounting

At the inception of a hedging relationship, the consolidated entity documents the relationship between the hedging instruments and hedged items, its risk management objective and its strategy for undertaking the hedge. The consolidated entity also requires a documented assessment, both at hedge inception and on an ongoing basis, of whether or not the derivatives that are used in hedging transactions are highly effective in offsetting the changes attributable to the hedged risks in the fair values or cash flows of hedged items. Interest on designated qualifying hedges is included in 'Net interest income'.

#### Fair value hedge

Fair value hedge accounting does not change the recording of gains and losses on derivatives and other hedging instruments, but results in recognising changes in the fair value of the hedged assets or liabilities attributable to the hedged risk that would not otherwise be recognised in the Income statement. If a hedge relationship no longer meets the criteria for hedge accounting, hedge accounting is discontinued; the cumulative adjustment to the carrying amount of the hedged item is amortised to the Income statement on a recalculated effective interest rate, unless the hedged item has been derecognised, in which case it is recognised in the Income statement immediately.

#### Cash flow hedge

The effective portion of gains and losses on hedging instruments is recognised in other comprehensive income; the ineffective portion of the change in fair value of derivative hedging instruments that are part of a cash flow hedge relationship is recognised immediately in the Income statement within 'Net trading income'. The accumulated gains and losses recognised in other comprehensive income are reclassified to the Income statement in the same periods in which the hedged item affects profit or loss. In hedges of forecast transactions that result in recognition of a non-financial asset or liability, previous gains and losses recognised in other comprehensive income are included in the initial measurement of the asset or liability. When a hedge relationship is discontinued, or partially discontinued, any cumulative gain or loss recognised in other comprehensive income remains in equity until the forecast transaction is recognised in the Income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss previously recognised in other comprehensive income is immediately reclassified to the Income statement.

#### Hedge effectiveness testing

To qualify for hedge accounting, the Bank requires that at the inception of the hedge and throughout its life, each hedge must be expected to be highly effective both prospectively and retrospectively, on an ongoing basis.

The documentation of each hedging relationship sets out how the effectiveness of the hedge is assessed and the method adopted by an entity to assess hedge effectiveness will depend on its risk management strategy. For prospective effectiveness, the hedging instrument must be expected to be highly effective in offsetting changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated, with the effectiveness range being defined as 80% to 125%. Hedge ineffectiveness is recognised in the Income statement in 'Net trading income'.

#### Derivatives that do not qualify for hedging

Non-qualifying hedges are derivatives entered into as economic hedges of assets and liabilities for which hedge accounting is not applied.

### (m) Derecognition of financial assets and liabilities

Financial assets are derecognised when the rights to receive cash flows from the assets have expired; or when the consolidated entity has transferred its contractual rights to receive the cash flows of the financial assets, and substantially all the risks and rewards of ownership; or where control is not retained.

Financial liabilities are derecognised when they are extinguished, that is when the obligation is discharged, cancelled or expires.

## **(n) Offsetting financial assets and financial liabilities**

Financial assets and financial liabilities are offset and the net amount reported in the Statement of financial position when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously.

## **(o) Goodwill**

Goodwill arises on business combinations when the cost of acquisition exceeds the fair value of the consolidated entity's share of the identifiable assets, liabilities and contingent liabilities acquired.

Goodwill is allocated to cash-generating units ('CGUs') for the purpose of impairment testing, which is undertaken at the lowest level at which goodwill is monitored for internal management purposes. Impairment testing is performed at least annually, and whenever there is an indication that the CGU may be impaired, by comparing the recoverable amount of a CGU with the carrying amount of its net assets, including attributable goodwill. The recoverable amount of an asset is the higher of its fair value less cost to sell, and its value in use. Value in use is the present value of the expected future cash flows from a CGU. If the recoverable amount of the CGU is less than the carrying value, an impairment loss is charged to the Income statement. Any write-off in excess of the carrying value of goodwill is limited to the fair value of the individual assets and liabilities of the CGU.

Goodwill is stated at cost, less accumulated impairment losses, which are charged to the Income statement (see note 13).

At the date of disposal of a business, attributable goodwill is included in the consolidated entity's share of net assets in the calculation of the gain or loss on disposal.

## **(p) Property, plant and equipment**

### **Recognition and measurement**

Items of property, plant and equipment are stated at cost less accumulated depreciation and impairment losses (see note 11).

Cost includes expenditures that are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for its intended use, and the cost of dismantling and removing the items and restoring the site on which they are located.

Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

Where parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items of property, plant and equipment.

### **Subsequent costs**

The consolidated entity recognises in the carrying amount of an item of property, plant and equipment the cost of replacing part of such an item when that cost is incurred if it is probable that the future economic benefits embodied with the item will flow to the consolidated entity and the cost of the item can be measured reliably. All other costs are recognised in the Income statement as an expense as incurred.

### **Depreciation**

Depreciation is charged to the Income statement on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment. The estimated useful lives in the current and comparative periods are as follows:

Plant and equipment	3-5 years
Fixtures and fittings	3-5 years
Leasehold improvements	life of the leasehold

The residual value, the useful life and the depreciation method applied to an asset are reassessed at least annually.

## **(q) Income tax**

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the Income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

HSBC Australia Holdings Pty Ltd and its wholly-owned Australian resident entities which include the Company have formed a tax-consolidated Group with effect from 1 July 2002 and are therefore taxed as a single entity from that date. The head entity within the tax-consolidated Group is HSBC Australia Holdings Pty Limited.

The following temporary differences are not provided for: initial recognition of goodwill, the initial recognition of assets or liabilities in a transaction that is not a business combination and that affect neither accounting nor taxable profit and differences relating to investments in subsidiaries to the extent that they probably will not reverse in the foreseeable future.

In determining the amount of current and deferred tax the consolidated entity takes into account the impact of uncertain tax positions and whether additional taxes and interest may be due. The consolidated entity believes that its accruals for tax liabilities are adequate for all open years based on its assessment of many factors, including interpretations of tax laws and prior experience. This assessment relies on estimates and assumptions and may involve a series of judgements about future events. New information may become available that causes the consolidated entity to change its judgement regarding the adequacy of its existing tax liabilities, such changes to tax liabilities will impact tax expense in the period that the determination is made.

Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

## Notes on the Consolidated Financial Statements

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

The current and deferred tax amounts for the tax-consolidated Group are allocated among the entities in the Group using a 'separate taxpayer within group' approach whereby each entity in the tax-consolidated group measures its current and deferred taxes as if it continued to be a separately taxable entity in its own right. Intercompany transactions are not eliminated.

Any current tax liabilities (or assets) and deferred tax assets arising from unused tax losses assumed by the head entity from the subsidiaries in the tax-consolidated group are recognised in conjunction with any tax funding arrangement amounts (refer below). Any difference between these amounts is recognised by the Company as an equity contribution from or distribution to the head entity.

The members of the tax-consolidated group have entered into a tax funding agreement which sets out the funding obligations of members of the tax-consolidated group in respect of tax amounts. The tax funding agreement requires payments equal to the current tax liability (asset) assumed by the head entity and any tax-loss deferred tax asset assumed by the head entity.

The members of the tax-consolidated group have also entered into a valid Tax Sharing Agreement under the tax consolidation legislation which sets out the allocation of income tax liabilities between the entities should the head entity default on its tax payment obligations and the treatment of entities leaving the tax consolidated group.

The Company recognises deferred tax assets arising from unused tax losses of the tax-consolidated group to the extent that it is probable that future taxable profits of the tax-consolidated group will be available against which the asset can be utilised.

Any subsequent period adjustments to deferred tax assets arising from unused tax losses as a result of revised assessments of the probability of recoverability is recognised by the head entity only.

### **(r) Goods and services tax**

Revenue, expenses and assets are recognised net of the amount of Goods and Services Tax ('GST'), except where the amount of GST incurred is not recoverable from the taxation authority. In these circumstances, the GST is recognised as part of the cost of acquisition of the asset or as part of the expense.

Receivables and payables are stated with the amount of GST included. The net amount of GST recoverable from, or payable to, the Australian Tax Office is included as a current asset or liability in the Statement of financial position.

Cash flows are included in the Statement of cash flows on a gross basis. The GST components of cash flows arising from investing and financing activities, which are recoverable from, or payable to, the Australian Tax Office are classified as operating cash flows.

### **(s) Employee benefits**

#### **Defined contribution plans**

Obligations for contributions to defined contribution pension plans are recognised as an expense in the Income statement as incurred.

#### **Long-term service benefits**

The liability for employee entitlements to long service leave represents the present value of the estimated future cash outflows to be made by the employer resulting from employees' services provided up to the reporting date. The provision has been calculated using estimated future increases in wage and salary rates, including related on-costs, and is discounted using the corporate bond rate.

#### **Share-based payments**

The cost of share-based payment arrangements with employees is measured by reference to the fair value of equity instruments on the date they are granted, and is recognised as an expense on a straight-line basis over the vesting period. The fair value of equity instruments that are made available immediately, with no vesting period attached to the award, are expensed immediately.

HSBC Holdings plc is the grantor of its equity instruments for all share awards and share options across the HSBC Group. The credit to 'Other reserves' over the vesting period on expensing an award represents the effective capital contribution from HSBC Holdings plc. To the extent the Bank will be, or has been, required to fund a share-based payment arrangement, this capital contribution is reduced and the fair value of shares expected to be released to employees is recorded within 'Other liabilities'.

Fair value is determined by using appropriate valuation models, taking into account the terms and conditions upon which the equity instruments were granted. Market performance conditions are taken into account when estimating the fair value of equity instruments at the date of grant, so that an award is treated as vesting irrespective of whether the market performance condition is satisfied, provided all other conditions are satisfied.

Vesting conditions, other than market performance conditions, are not taken into account in the initial estimate of the fair value at the grant date. They are taken into account by adjusting the number of equity instruments included in the measurement of the transaction, so that the amount recognised for services received as consideration for the equity instruments granted shall be based on the number of equity instruments that eventually vest. On a cumulative basis, no expense is recognised for equity instruments that do not vest because of a failure to satisfy non-market performance or service conditions.

A cancellation that occurs during the vesting period is treated as an acceleration of vesting and recognised immediately for the amount that would otherwise have been recognised for services over the remaining vesting period.

#### **Termination benefits**

Termination benefits are recognised as an expense when the consolidated entity is demonstrably committed, without realistic possibility of withdrawal, to a formal detailed plan to terminate employment before the normal retirement date. Termination benefits for voluntary redundancies are recognised if the consolidated entity has made an offer encouraging voluntary redundancy, it is probable that the offer will be accepted, and the number of acceptances can be estimated reliably.

### **(t) Provisions for liabilities and charges**

Provisions are recognised when it is probable that an outflow of economic benefits will be required to settle a present legal or constructive obligation that has arisen as a result of past events and for which a reliable estimate can be made.

The recognition and measurement of provisions requires the Bank to make a number of judgements, assumptions and estimates. The most significant are set out below:

Judgements	Estimates
<ul style="list-style-type: none"> <li>Determining whether a present obligation exists. Professional advice is taken on the assessment of litigation, property (including onerous contracts) and similar obligations</li> <li>Provisions for legal proceedings and regulatory matters typically require a higher degree of judgement than other types of provisions. When matters are at an early stage, accounting judgements can be difficult because of the high degree of uncertainty associated with determining whether a present obligation exists, and estimating the probability and amount of any outflows that may arise. As matters progress, management and legal advisers evaluate on an ongoing basis whether provisions should be recognised, revising previous estimates as appropriate. At more advanced stages, it is typically easier to make estimates around a better defined set of possible outcomes</li> </ul>	<ul style="list-style-type: none"> <li>Provisions for legal proceedings and regulatory matters remain very sensitive to the assumptions used in the estimate. There could be a wider range of possible outcomes for any pending legal proceedings, investigations or inquiries. As a result it is often not practicable to quantify a range of possible outcomes for individual matters. It is also not practicable to meaningfully quantify ranges of potential outcomes in aggregate for these types of provisions because of the diverse nature and circumstances of such matters and the wide range of uncertainties involved</li> <li>Provisions for customer remediation also require significant levels of estimation. The amounts of provisions recognised depend on a number of different assumptions and where appropriate assessed on activity, process, type of service or product and where applicable on an individual basis. More information about these assumptions is included in note 17</li> </ul>

## Contingent liabilities, contractual commitments and guarantees

Contingent liabilities, which include certain guarantees and letters of credit pledged as collateral security, and contingent liabilities related to legal proceedings or regulatory matters, are not recognised in the financial statements but are disclosed unless the probability of settlement is remote.

### (u) Financial guarantees

Liabilities under financial guarantee contracts which are not classified as insurance contracts are recorded initially at their fair value, which is generally the fee received or receivable. Subsequently, financial guarantee liabilities are measured at the higher of the initial fair value, less cumulative amortisation, and the best estimate of the expenditure required to settle the obligations.

### Debt securities on issue and subordinated liabilities

Debt securities issued for trading purposes or designated at fair value are reported under the appropriate Statement of financial position captions. Other debt securities on issue and subordinated liabilities are measured at amortised cost using the effective interest method and are reported under 'Debt securities on issue' or 'Subordinated liabilities'.

### (v) Cash and cash equivalents

For the purpose of the Statement of cash flows, cash and equivalents include highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value. Such investments comprise cash and balances with banks maturing within one month, and treasury bills and certificates of deposit with less than three months' maturity from the date of acquisition.

### (w) Share capital and other capital instruments

Shares and other financial instruments are classified as equity when the Bank has the unconditional right to avoid transferring cash or other financial assets to the holder. Incremental costs directly attributable to the issue of equity instruments are shown in equity as a deduction from the proceeds, net of tax. The additional tier 1 capital instruments are perpetual subordinated loans on which coupon payments may be cancelled at the sole discretion of the Bank. The subordinated loans will be written down at the point of non-viability on the occurrence of a trigger event as defined in the banking (capital) rules. They rank higher than ordinary shares in the event of a wind-up.

### (x) Intangible assets

The Bank develops a number of internally generated software assets which are used in order to generate income across the operations of these assets. The Bank generates business cases during the research phase of the development and this forms the basis of the approval to proceed with the development of the internally generated software. Intangible assets with finite useful lives are generally amortised, on a straight-line basis, over their useful lives of between three and five years. The amortisation period and amortisation method for an intangible asset with a finite useful life is reviewed at least at each financial year-end.

### (y) Leases

The Bank leases various offices across multiple sites. Rental contracts are typically made for fixed period and may include extension options. Lease terms are negotiated on an individual basis and contain a wide range of different terms and conditions. Leases are recognised as a right-of-use asset (ROU) and corresponding liability at the date at which the leased asset is available for use by the Bank. Assets and liabilities arising from a lease are initially measured on a present value basis. Lease payments to be made under reasonably certain extension options are included in the measurement of the liability. The discount rate used is the incremental borrowing rate should the Bank have to borrow the funds. The Bank is exposed to potential future increases in variable lease payments based on an index or rate, which are not included in the lease liability until they take effect. When adjustments to lease payments based on an index or rate take effect, the lease liability is reassessed and adjusted against the ROU asset. ROU assets are generally depreciated over the shorter of the asset's useful life and the lease term on a straight-line basis. Payments on low-value assets are recognised on a straight line basis as an expense.

## 4 Net operating income

		Consolidated		Company	
		2020	2019	2020	2019
	Notes	\$m	\$m	\$m	\$m
<b>(i) Interest income</b>					
Loans and advances to banks		5.8	20.7	5.8	20.7
Loans and advances to customers		831.8	967.6	831.8	967.6
Financial assets measured at FVOCI		85.9	192.2	85.9	192.2
Related corporations		1.4	5.7	1.4	5.7
Key management personnel		0.2	0.2	0.2	0.2
		925.1	1,186.4	925.1	1,186.4
<b>(ii) Interest expense</b>					
Deposits by banks		1.7	3.8	1.7	3.8
Customer accounts		167.3	324.6	167.3	324.6
Repurchase agreements		5.1	17.2	5.1	17.2
Debt securities on issue		4.1	7.3	1.1	7.3
Related corporations		27.7	73.0	30.7	73.0
Lease liability		9.2	7.4	9.2	7.4
Other interest		0.7	—	0.7	—
<b>Total interest expense</b>		<b>215.8</b>	<b>433.3</b>	<b>215.8</b>	<b>433.3</b>
Less					
Interest expense classified as 'Net loss from financial instruments designated at fair value'	4(vii)	(1.6)	(1.3)	(1.6)	(1.3)
<b>Interest expense</b>		<b>214.2</b>	<b>432.0</b>	<b>214.2</b>	<b>432.0</b>
<b>(iii) Other operating income</b>					
Recharge to related corporations		146.0	149.5	146.0	149.5
Loss on sale of loans at amortised cost		(7.9)	—	(7.9)	
Other income		2.5	3.5	2.5	3.5
		140.6	153.0	140.6	153.0
<b>(iv) Fee and commission income</b>					
Fees and commissions		149.5	162.0	149.5	162.0
Fee income on fiduciary activities		17.0	16.5	17.0	16.5
		166.5	178.5	166.5	178.5
<b>(v) Fee and commission expense</b>					
Fees and commissions		60.3	57.9	60.3	57.9
Fees payable on fiduciary activities		2.0	3.2	2.0	3.2
		62.3	61.1	62.3	61.1
<b>(vi) Net trading income</b>					
Exchange rates		95.1	110.6	95.1	110.6
Interest rates		(0.1)	(0.1)	(0.1)	(0.1)
		95.0	110.5	95.0	110.5
Gains/(losses) from hedging activities					
Fair value hedges					
Net loss on hedged items attributable to the hedged risk		(54.1)	(51.1)	(54.1)	(51.1)
Net gain on hedging instruments		54.2	48.3	54.2	48.3
		0.1	(2.8)	0.1	(2.8)
Net interest income on trading activities					
Interest income		—	0.2	—	0.2
<b>Total net trading income</b>		<b>95.1</b>	<b>107.9</b>	<b>95.1</b>	<b>107.9</b>
<b>(vii) Net loss from financial instruments designated at fair value</b>					
Net loss from financial instruments designated at fair value		—	(0.2)	—	(0.2)
Net interest expense on financial instruments designated at fair value	4(iii)	(1.6)	(1.3)	(1.6)	(1.3)
<b>Total net loss from financial instruments designated at fair value</b>		<b>(1.6)</b>	<b>(1.5)</b>	<b>(1.6)</b>	<b>(1.5)</b>
<b>(viii) Net gain from disposal of financial assets measured at fair value through other comprehensive income</b>					
Net gain from disposal of financial assets measured at at fair value through other comprehensive income		27.2	37.1	27.2	37.1



## 5 Net change in expected credit losses and other credit risk provisions

	Consolidated		Company	
	2020	2019	2020	2019
	\$m	\$m	\$m	\$m
<b>Loans and advances to banks and customers</b>				
New allowances net of allowance releases	(46.4)	(2.3)	(46.4)	(2.3)
Recoveries of amounts previously written off	7.0	5.6	7.0	5.6
Loan commitments and guarantees and other financial assets	(6.0)	4.1	(6.0)	4.1
Debt instruments measured at fair value through other comprehensive income	(0.8)	(0.1)	(0.8)	(0.1)
<b>Net change in expected credit losses and other credit risk provisions</b>	<b>(46.2)</b>	<b>7.3</b>	<b>(46.2)</b>	<b>7.3</b>

## 6 Operating expenses

	Notes	Consolidated		Company	
		2020	2019	2020	2019
		\$m	\$m	\$m	\$m
<b>Employee compensation and benefits</b>					
Wages and salaries		232.0	218.5	232.0	218.5
Bonuses		46.2	53.3	46.2	53.3
Retirement and termination benefits		24.0	27.5	24.0	27.5
Share-based payment transactions	20	4.0	4.7	4.0	4.7
Other		28.1	26.9	28.1	26.9
		<b>334.3</b>	<b>330.9</b>	<b>334.3</b>	<b>330.9</b>
<b>Premises and equipment</b>					
Property rental		11.4	14.1	11.4	14.1
Equipment and other premise expense		4.7	7.2	4.7	7.2
Depreciation		48.9	44.7	48.9	44.7
		<b>65.0</b>	<b>66.0</b>	<b>65.0</b>	<b>66.0</b>
<b>General and administrative expenses</b>					
Marketing and communication		33.9	38.9	33.9	38.9
Legal and professional expenses		18.5	21.7	18.5	21.7
Printing and communication costs		12.6	14.7	12.6	14.7
Travel and entertainment		2.4	6.9	2.4	6.9
Auditor's remuneration		2.2	2.2	2.2	2.2
Fraud and operational losses		8.0	6.9	8.0	6.9
Contracted services		24.7	31.2	24.7	31.2
Other		22.9	19.2	22.9	19.2
		<b>125.2</b>	<b>141.7</b>	<b>125.2</b>	<b>141.7</b>
<b>Other expenses</b>					
Intercompany management fees	33	185.5	157.7	185.5	157.7
Amortisation of intangibles		5.2	4.7	5.2	4.7
		<b>190.7</b>	<b>162.4</b>	<b>190.7</b>	<b>162.4</b>

## 7 Auditor's remuneration

	Consolidated		Company	
	2020	2019	2020	2019
	\$	\$	\$	\$
<b>Auditor of the consolidated entity</b>				
<b>Audit services</b>				
Audit and review of financial reports	1,093,257	1,100,548	1,093,257	1,100,548
<b>Other assurance services</b>				
Regulatory and other audit services	1,102,153	1,102,153	1,102,153	1,102,153
	<b>2,195,410</b>	<b>2,202,701</b>	<b>2,195,410</b>	<b>2,202,701</b>

## 8 Income tax expense

	Notes	Consolidated		Company	
		2020	2019	2020	2019
		\$m	\$m	\$m	\$m
<b>Recognised in the Income statement</b>					
<b>(a) Current tax expense</b>					
Current year		(111.9)	(139.2)	(111.9)	(139.2)
Adjustments for prior years		6.9	2.8	6.9	2.8
		(105.0)	(136.4)	(105.0)	(136.4)
<b>Deferred tax expense</b>					
Origination and reversal of temporary differences		16.6	(4.5)	16.6	(4.5)
Adjustments for prior years		(6.3)	(3.1)	(6.3)	(3.1)
	15	10.3	(7.6)	10.3	(7.6)
<b>Total income tax expense in Income statement</b>					
Attributable to continuing operations		(94.7)	(144.0)	(94.7)	(144.0)
<b>Numerical reconciliation between income tax expense and pre-tax net profit</b>					
<b>Profit before income tax</b>					
		315.0	474.4	315.0	474.4
Income tax using the corporation tax rate of 30%		(94.5)	(142.3)	(94.5)	(142.3)
(Increase)/decrease in income tax expense due to:					
– non-deductible expenses		(0.8)	(1.4)	(0.8)	(1.4)
		(95.3)	(143.7)	(95.3)	(143.7)
(Under)/over provided in prior years		0.6	(0.3)	0.6	(0.3)
<b>Income tax expense</b>					
		(94.7)	(144.0)	(94.7)	(144.0)
<b>(b) Deferred tax recognised directly in equity</b>					
Relating to capital contribution reserve		(0.5)	0.2	(0.5)	0.2
Relating to financial assets measured at FVOCI and cash flow hedging reserves		(10.2)	(5.5)	(10.2)	(5.5)
	15	(10.7)	(5.3)	(10.7)	(5.3)

## 9 Derivatives

Derivatives are financial instruments that derive their value from the price of an underlying item such as equities, bonds, interest rates, foreign exchange, credit spreads, commodities and equity or other indices.

Derivatives enable users to increase, reduce or alter exposure to credit or market risks. The consolidated entity makes markets in derivatives for its customers and uses derivatives to manage its exposure to credit and market risks.

Derivatives are carried at fair value and shown in the Statement of financial position as separate totals of assets and liabilities. A description of how the fair value of derivatives is derived is set out in note 28.

Derivative assets and liabilities on different transactions are only offset if: the transactions are with the same counterparty, a legal right of set-off exists and the cash flows are intended to be settled on a net basis. Changes in the values of derivatives are recognised in accordance with the consolidated entity's accounting policy as described in note 3(l).

### Use of derivatives

The consolidated entity transacts derivatives for two primary purposes: to create risk management solutions for clients; and to manage and hedge the consolidated entity's own risks. For accounting purposes, derivative instruments are classified as held either for trading or hedging. Derivatives that are held as hedging instruments are formally designated as hedges as defined in AASB 9. All other derivative instruments are classified as held-for-trading. The held-for-trading classification includes two types of derivative instruments. The first type are those used in sales and trading activities, and those instruments that are used for risk management purposes but which for various reasons do not meet the qualifying criteria for hedge accounting. The second type of held-for-trading category includes derivatives managed in conjunction with financial instruments designated at fair value. These activities are described more fully below.

Derivative positions are managed constantly to ensure that they remain within acceptable risk levels, with offsetting deals being utilised to achieve this where necessary. When entering into derivative transactions, the consolidated entity employs the same credit risk management procedures to assess and approve potential credit exposures as are used for traditional lending.

### Trading derivatives

Most of the consolidated entity's derivative transactions relate to sales. Sales activities include the structuring and marketing of derivative products to customers to enable them to take, transfer, modify or reduce current or expected risks.

As mentioned above, other derivatives classified as held-for-trading include: non-qualifying hedging derivatives; ineffective hedging derivatives; and the components of hedging derivatives that are excluded from assessing hedge effectiveness. Non-qualifying hedging derivatives are entered into for risk management purposes but do not meet the criteria for hedge accounting. These include derivatives managed in conjunction with financial instruments designated at fair value. Ineffective hedging derivatives were previously designated as hedges, but no longer meet the criteria for hedge accounting.

### Hedging derivatives

The consolidated entity uses derivatives (principally interest rate swaps) for hedging purposes in the management of its own asset and liability portfolios and structural positions. This enables the consolidated entity to optimise the overall cost of accessing debt capital markets, and to mitigate the market risk, which would otherwise arise from structural imbalances in the maturity and other profiles of its assets and liabilities.

The accounting treatment of hedge transactions varies according to the nature of the instrument hedged and the type of hedge transactions. Derivatives may qualify as hedges for accounting purposes if they are fair value hedges or cash flow hedges.



The cash flows of the above hedging derivatives are not expected to affect the Income statement in 2020 and beyond.

With respect to exchange rate and interest rate contracts, the notional or contractual amounts of these instruments indicate the nominal value of transactions outstanding at the reporting date; they do not represent amounts at risk.

## Offsetting

Offsetting can occur in the following instances:

- the counterparty has an offsetting exposure with the banks and a master netting or similar arrangement is in place with a right to set off only in the event of default, insolvency or bankruptcy, or the offset criteria are otherwise not satisfied; and
- in the case of derivatives and reverse repurchase/repurchase, stock borrowing/lending and similar agreements, cash and non-cash collateral has been received/pledged.

For risk management purposes, the net amounts of loans and advances to customers are subject to limits, which are monitored and the relevant customer agreements are subject to review and updated, as necessary, to ensure that the legal right to set off remains appropriate.

The bank has \$2,046.9m (2019: \$4,022.7m) in repurchase agreements with enforceable netting arrangements, \$256.5m (2019: \$55.5m) in derivatives.

## Fair value of open positions by product type

The following table summarises the fair values of third party and inter-company derivatives' open positions by product contract type.

### Fair values of third party and inter-company derivatives' open positions by product contract type

	Consolidated		Company	
	2020 \$m	2019 \$m	2020 \$m	2019 \$m
<b>Assets</b>				
<b>Trading derivatives</b>				
Third party				
– exchange rate	78.2	30.2	78.2	30.2
– interest rate	3.6	4.6	3.6	4.6
	81.8	34.8	81.8	34.8
<b>Related entities</b>				
– exchange rate	94.0	34.0	94.0	34.0
– interest rate	2.9	3.4	2.9	3.4
	96.9	37.4	96.9	37.4
<b>Hedging derivatives</b>				
<b>Related entities</b>				
– interest rate	–	2.3	–	2.3
	–	2.3	–	2.3
	178.7	74.5	178.7	74.5
<b>Liabilities</b>				
<b>Trading derivatives</b>				
Third party				
– exchange rate	93.6	32.8	93.6	32.8
– interest rate	0.1	0.3	0.1	0.3
	93.7	33.1	93.7	33.1
<b>Related entities</b>				
– exchange rate	151.4	53.4	151.4	53.4
– interest rate	3.8	4.8	3.8	4.8
	155.2	58.2	155.2	58.2
<b>Hedging derivatives</b>				
<b>Related entities</b>				
– interest rate	111.0	68.9	111.0	68.9
	359.9	160.2	359.9	160.2

## Fair value hedges

The consolidated entity's fair value hedges principally consist of interest rate swaps that are used to protect against changes in the fair value of fixed-rate long-term financial instruments due to movements in market interest rates.

For qualifying fair value hedges, all changes in the fair value of the derivative and in the fair value of the item in relation to the risk being hedged are recognised in income. If the hedge relationship is terminated, the fair value adjustment to the hedged item continues to be reported as part of the basis of the item and is amortised to income as a yield adjustment over the remainder of the hedging period.

The fair values of outstanding derivatives designated as fair value hedges at 31 December 2020 were assets of Nil (2019: \$2.3m) and liabilities of \$111.0m (2019: \$68.4m).

## Notes on the Consolidated Financial Statements

### Gains or losses arising from fair value hedges

	Consolidated		Company	
	2020 \$m	2019 \$m	2020 \$m	2019 \$m
<b>Gains or losses arising from fair value hedges</b>				
Gains/(losses)				
– on hedging instruments	(54.1)	(51.1)	(54.1)	(51.1)
– on hedged items attributable to the hedged risk	54.2	48.3	54.2	48.3
	<b>0.1</b>	<b>(2.8)</b>	<b>0.1</b>	<b>(2.8)</b>

### Cash flow hedges

The consolidated entity is exposed to variability in future interest cash flows on non-trading assets and liabilities which bear interest at variable rates or which are expected to be re-funded or reinvested in the future. The amounts and timing of future cash flows, representing both principal and interest flows, are projected for each portfolio of financial assets and liabilities on the basis of their contractual terms and other relevant factors, including estimates of prepayments and defaults. The aggregate principal balances and interest cash flows across all portfolios over time form the basis for identifying gains and losses on the effective portions of derivatives designated as cash flow hedges. These are initially recognised directly in equity as gains or losses not recognised in the Income statement and are transferred to current period earnings when the forecast cash flows affect net profit or loss.

At 31 December 2020, the fair values of outstanding derivatives designated as cash flow hedges were assets of Nil (2019: Nil) and liabilities of Nil (2019: \$0.6m).

The schedule of forecast principal balances on which the expected interest cash flows arise as at 31 December 2020 is as follows:

### Forecast principal balances on which interest cash flows are expected to arise – Consolidated and Company

	3 months or less \$m	More than 3 months but less than 1 year \$m	5 years or less but more than 1 year \$m
<b>At 31 Dec 2020</b>			
Cash inflows exposures			
Cash outflows exposures	(100.0)	(100.0)	(100.0)
<b>Net cash inflows/(outflows)</b>	<b>(100.0)</b>	<b>(100.0)</b>	<b>(100.0)</b>
<b>At 31 Dec 2019</b>			
Cash inflows exposures	—	—	—
Cash outflows exposures	(150.0)	—	—
<b>Net cash inflows/(outflows)</b>	<b>(150.0)</b>	<b>—</b>	<b>—</b>

## 10 Financial assets measured at fair value through other comprehensive income

	Consolidated		Company	
	2020 \$m	2019 \$m	2020 \$m	2019 \$m
Analysis of financial assets measured at FVOCI by security type				
– debt securities	8,656.5	8,105.2	8,656.5	8,105.2
– equities	4.4	4.0	4.4	4.0
– treasury and other eligible bills	3,399.8	3,374.6	3,399.8	3,374.6
	<b>12,060.7</b>	<b>11,483.8</b>	<b>12,060.7</b>	<b>11,483.8</b>
Analysis of financial assets measured at FVOCI by security issuer				
– government securities and Australian Government agencies	10,461.6	9,523.2	10,461.6	9,523.2
– banks and building societies	1,599.1	1,960.6	1,599.1	1,960.6
	<b>12,060.7</b>	<b>11,483.8</b>	<b>12,060.7</b>	<b>11,483.8</b>

## 11 Property, plant and equipment

	Consolidated		Company	
	2020 \$m	2019 \$m	2020 \$m	2019 \$m
<b>Leasehold improvements at cost</b>				
Balance at 1 Jan	90.8	80.3	90.8	80.3
Assets acquired	10.6	10.5	10.6	10.5
Assets disposed	—	—	—	—
<b>Balance at 31 Dec</b>	<b>101.4</b>	<b>90.8</b>	<b>101.4</b>	<b>90.8</b>
<b>Furniture, fittings, office equipment at cost</b>				
Balance at 1 Jan	24.9	20.0	24.9	20.0
Assets acquired	3.7	4.9	3.7	4.9
Assets disposed	—	—	—	—
<b>Balance at 31 Dec</b>	<b>28.6</b>	<b>24.9</b>	<b>28.6</b>	<b>24.9</b>
<b>Leasehold improvements accumulated depreciation</b>				
Balance at 1 Jan	(54.6)	(50.1)	(54.6)	(50.1)
Depreciation charge for the year	(5.9)	(4.5)	(5.9)	(4.5)
Disposals	—	—	—	—
<b>Balance at 31 Dec</b>	<b>(60.5)</b>	<b>(54.6)</b>	<b>(60.5)</b>	<b>(54.6)</b>
<b>Furniture, fittings, office equipment accumulated depreciation</b>				
Balance at 1 Jan	(17.0)	(14.4)	(17.0)	(14.4)
Depreciation charge for the year	(3.6)	(2.6)	(3.6)	(2.6)
Disposals	—	—	—	—
<b>Balance at 31 Dec</b>	<b>(20.6)</b>	<b>(17.0)</b>	<b>(20.6)</b>	<b>(17.0)</b>
<b>Carrying amounts</b>				
At 1 Jan	44.1	35.8	44.1	35.8
<b>At 31 Dec</b>	<b>48.9</b>	<b>44.1</b>	<b>48.9</b>	<b>44.1</b>

## 12 Group entities

	Notes	2020 %	2019 %	Place of incorporation
<b>Controlling entity</b>				
HSBC Bank Australia Limited		—	—	Australia
<b>Controlled entities</b>				
HSBC Custody Nominees (Australia) Limited		100	100	Australia
Lion Series 2009-1 Trust	1	100	100	Australia
Lion Series 2020 -1 Trust	2	100	—	Australia

- 1 The Company established the Lion 2009-1 Trust in July 2009 to enable the creation of notes eligible for sale and repurchase with the RBA, as part of the consolidated entity's contingency liquidity plan. The Company does not hold any ownership interests in Lion Series 2009-1 Trust. It owns all the notes and receives substantially all of the benefits related to the Lion Trust securitisation programme. As a result, the Company consolidates this entity.
- 2 The Company established the Lion 2020-1 Trust in August 2020 to enable the securitisation of residential mortgages with notes issued to external investors. Although the Company does not hold any ownership interests in Lion Trust 2020-1, it receives substantially all of the benefits related to the Lion Trust securitisation programme. Consequently, the Company consolidates this entity. Further details are contained in Note 31.

## 13 Intangible assets

	Consolidated		Company	
	2020 \$m	2019 \$m	2020 \$m	2019 \$m
<b>Goodwill</b>				
Cost and carrying amount				
Balance at 1 Jan	58.7	58.7	58.7	58.7
<b>Balance at 31 Dec</b>	<b>58.7</b>	<b>58.7</b>	<b>58.7</b>	<b>58.7</b>
<b>Internally generated software</b>				
Cost				
Balance at 1 Jan	33.1	27.0	33.1	27.0
Addition	1.4	6.1	1.4	6.1
<b>Balance at 31 Dec</b>	<b>34.5</b>	<b>33.1</b>	<b>34.5</b>	<b>33.1</b>
<b>Accumulated amortisation</b>				
Balance at 1 Jan	(18.7)	(14.0)	(18.7)	(14.0)
Amortisation charge for the year	(5.3)	(4.7)	(5.3)	(4.7)
<b>Balance at 31 Dec</b>	<b>(24.0)</b>	<b>(18.7)</b>	<b>(24.0)</b>	<b>(18.7)</b>
<b>Carrying amounts</b>				
At 1 Jan	14.4	13.0	14.4	13.0
<b>At 31 Dec</b>	<b>10.5</b>	<b>14.4</b>	<b>10.5</b>	<b>14.4</b>
<b>Total intangible assets</b>	<b>69.2</b>	<b>73.1</b>	<b>69.2</b>	<b>73.1</b>

## Notes on the Consolidated Financial Statements

### Segment allocation of goodwill

In accordance with Australian Accounting Standard AASB 138 'Intangible Assets', the consolidated entity's carrying amount of goodwill as at 31 December 2020 is disclosed for each segment of business.

	Consolidated		Company	
	2020 \$m	2019 \$m	2020 \$m	2019 \$m
Wealth and Personal Banking	57.4	57.4	57.4	57.4
Global Banking and Markets	1.3	1.3	1.3	1.3
	58.7	58.7	58.7	58.7

### Impairment tests for goodwill

Goodwill has been allocated for impairment testing purposes to cash generating units in the following business segments: Wealth and Personal Banking, and Global Banking and Markets. Under AASB 136 'Impairment of assets', a cash-generating unit to which goodwill has been allocated shall be tested for impairment annually, and whenever there is an indication that the unit may be impaired. At 31 December 2020 we considered the pervasive macroeconomic deterioration caused by the outbreak of COVID-19, along with the impact on forecast profitability, to be an indicator of goodwill impairment.

The key assumptions in calculating the recoverable amounts of these segments are disclosed below.

#### Wealth and Personal Banking Management

Goodwill allocated to Wealth and Personal Banking arose from the company's acquisition in 2001 of NRMA Building Society Group Limited. The Wealth and Personal Banking unit's impairment test is based on value in use calculations ('VIU').

The VIU is calculated by discounting management's cash flow projections for the CGU. The cash flow projections are based on the Board approved 5-year plan with cash flows in perpetuity extrapolated using a long-term growth rate because of the long-term perspective within the Bank. The long-term growth rate of 2.4% (2019: 2.6%) reflects nominal GDP and inflation and is based on a 20-year forecast or historical inflation data (whichever is lower).

The discount rate of 10.1% (2019: 7.8%) is based on the cost of capital the HSBC Group allocates to investments in the countries within which the CGU operates.

Our cash flow forecasts were updated for changes in the external outlook, although economic and geopolitical risks increase the inherent estimation uncertainty.

The forecasts applied by management are not reliant on any one particular assumption and there are no reasonably possible changes in assumptions for that would result in an indication of impairment.

#### Global Banking and Markets

The Global Banking and Markets impairment test is based on VIU calculations.

The business and associated clients that were purchased through an acquisition from State Street generated a net profit after tax during the year ended 31 December 2020 that exceeded the carrying amounts of the goodwill.

With a carrying goodwill value of \$1.3m, discounted cash flow models utilising both two- and five-year time spans and discount rates of BBSW resulted in a recoverable amount in excess of the carrying amount of the unit.

The recoverable amount exceeds the carrying amount of goodwill of \$1.3m, such that management considers that it is not reasonably possible for the assumed future earnings to change so significantly as to eliminate this excess.

## 14 Other assets

	Consolidated		Company	
	2020 \$m	2019 \$m	2020 \$m	2019 \$m
Acceptances and endorsements	19.7	17.9	19.7	17.9
Prepayments and accrued income	124.9	135.9	129.6	133.9
Margins with exchange	391.5	307.9	391.5	307.9
Other assets	28.4	20.7	28.4	19.9
Assets held for resale	4.4	5.7	4.4	5.7
<b>Total</b>	<b>568.9</b>	<b>488.1</b>	<b>573.6</b>	<b>485.3</b>

Assets held for resale mainly comprised assets acquired by repossession of collateral for realisation.

## 15 Tax assets and liabilities

### Current tax assets and liabilities

Both the Bank and the consolidated entity have no current tax assets or liabilities. In accordance with the tax legislation the immediate parent entity, HSBC Australia Holdings Pty Limited, as head entity of the tax consolidated has assumed the current tax liability/(asset) initially recognised by members in the tax consolidated Group and, in accordance with the Tax Funding Agreement, the members in the tax consolidated group recognise a corresponding intercompany (asset)/ liability to the head entity.

## Recognised deferred tax assets and liabilities

### Deferred tax assets and liabilities

	Deferred tax assets		Deferred tax liabilities		Net deferred tax assets	
	2020 \$m	2019 \$m	2020 \$m	2019 \$m	2020 \$m	2019 \$m
<b>Consolidated and Company</b>						
Impairment allowances	43.6	37.4	—	(1.1)	43.6	36.3
Tangible fixed assets	18.6	17.3	—	—	18.6	17.3
Prepayments and accrued income	0.2	—	(0.3)	(1.0)	(0.1)	(1.0)
Other assets	5.2	2.2	—	—	5.2	2.2
Other liabilities/accrued expenses	3.2	5.7	(1.8)	(1.3)	1.4	4.4
Accruals and deferred income	40.2	41.3	—	—	40.2	41.3
Provision for liabilities and charges	6.5	4.9	—	—	6.5	4.9
Retained earnings	0.3	0.8	—	—	0.3	0.8
Cash flow hedging reserve	—	0.2	—	—	—	0.2
Financial assets measured at FVOCI securities reserve	0.4	—	(14.8)	(4.7)	(14.4)	(4.7)
Own credit spread reserve	0.3	0.3	—	—	0.3	0.3
<b>Total tax assets/(liabilities)</b>	<b>118.5</b>	<b>110.1</b>	<b>(16.9)</b>	<b>(8.1)</b>	<b>101.6</b>	<b>102.0</b>

### Movement in temporary differences

	1 Jan 2020 \$m	Recognised in income \$m	Recognised in equity \$m	31 Dec 2020 \$m	1 Jan 2019 \$m	Recognised in income \$m	Recognised in equity \$m	31 Dec 2019 \$m
<b>Consolidated and Company</b>								
Impairment allowances	36.3	7.3	—	43.6	47.4	(11.1)	—	36.3
Tangible fixed assets	17.3	1.3	—	18.6	16.0	1.3	—	17.3
Prepayments and accrued income	(1.0)	0.9	—	(0.1)	(0.9)	(0.1)	—	(1.0)
Other assets	2.2	3.0	—	5.2	—	2.2	—	2.2
Other liabilities/accrued expenses	4.4	(3.0)	—	1.4	3.9	0.5	—	4.4
Accruals and deferred income	41.3	(1.1)	—	40.2	41.5	(0.2)	—	41.3
Provision for liabilities and charges	4.9	1.6	—	6.5	5.1	(0.2)	—	4.9
Retained earnings	0.8	—	(0.5)	0.3	0.6	—	0.2	0.8
Cash flow hedging reserve	0.2	—	(0.2)	—	1.1	—	(0.9)	0.2
FVOCI securities reserve	(4.7)	0.3	(10.0)	(14.4)	(0.1)	—	(4.6)	(4.7)
Own credit spread reserve	0.3	—	—	0.3	0.3	—	—	0.3
	<b>102.0</b>	<b>10.3</b>	<b>(10.7)</b>	<b>101.6</b>	<b>114.9</b>	<b>(7.6)</b>	<b>(5.3)</b>	<b>102.0</b>

## 16 Financial liabilities designated at fair value

	Consolidated		Company	
	2020 \$m	2019 \$m	2020 \$m	2019 \$m
<b>Financial liabilities designated at fair value</b>				
Debt securities on issue	43.2	43.7	43.2	43.7
	<b>43.2</b>	<b>43.7</b>	<b>43.2</b>	<b>43.7</b>

## 17 Provisions for liabilities and charges

	Consolidated		Company	
	2020 \$m	2019 \$m	2020 \$m	2019 \$m
<b>At 1 Jan</b>	<b>16.4</b>	<b>16.6</b>	<b>16.4</b>	<b>16.6</b>
New provisions	21.6	15.2	21.6	15.2
Release of provision	(14.7)	(8.9)	(14.7)	(8.9)
Provisions utilised	(1.6)	(6.5)	(1.6)	(6.5)
<b>At 31 Dec</b>	<b>21.7</b>	<b>16.4</b>	<b>21.7</b>	<b>16.4</b>

Provisions contain the ECL provision for off balance sheet items of \$10.7m (2019: \$9.4m) see note 27 and other provisions. Within the provisions above a customer remediation provision has been made and other individually insignificant provisions, in respect of restructuring and litigation.

## 18 Debt securities on issue

	Consolidated		Company	
	2020	2019	2020	2019
	\$m	\$m	\$m	\$m
Certificate of deposit	—	—	—	—
Bonds and medium-term notes	892.9	100.0	—	100.0
	892.9	100.0	—	100.0

## 19 Other liabilities

	Consolidated		Company	
	2020	2019	2020	2019
	\$m	\$m	\$m	\$m
Acceptances and endorsements	19.7	17.9	19.7	17.9
Accruals and deferred income	68.0	68.8	71.8	66.0
Settlement balances	32.4	47.8	32.4	47.8
Other liabilities	29.8	36.8	29.9	36.8
	149.9	171.3	153.8	168.5

## 20 Employee benefits

	Consolidated		Company	
	2020	2019	2020	2019
	\$m	\$m	\$m	\$m
Liability for annual leave	18.6	15.3	18.6	15.3
Bonus payable	48.3	52.3	48.3	52.3
Liability for long service leave	29.0	22.9	29.0	22.9
	95.9	90.5	95.9	90.5

### Defined contribution plans

The Company and the consolidated entity makes contributions to the staff superannuation scheme, a defined contribution plan.

The amount recognised as an expense was \$20.2m for the year ended 31 December 2020 (2019: \$19.7m).

### Share-based payments

The consolidated entity's key management personnel and employees participate in both discretionary and voluntary HSBC Holdings plc compensation plans. Discretionary share plans include performance and restricted/achievement share awards.

Sharesave and Sharematch are voluntary savings related share option plans for all eligible employees.

During 2020, \$4.0m (2019: \$4.7m) was charged to the Income statement by the Company and the consolidated entity in respect of share-based transactions settled in equity. This expense was computed from the fair values of the share-based payment transactions when contracted, arising under employee share awards made in accordance with HSBC Holdings plc's reward structures.

## 21 Share capital

	Consolidated		Company	
	2020	2019	2020	2019
	\$m	\$m	\$m	\$m
<b>Issued capital</b>				
685,250,305 ordinary shares fully paid	811.0	811.0	811.0	811.0
	811.0	811.0	811.0	811.0

### Ordinary shares

The holders of ordinary shares are entitled to receive dividends as declared from time to time and are entitled to one vote per share at shareholder meetings. In the event of winding up of the Company, ordinary shareholders rank after all creditors and are fully entitled to any proceeds of liquidation.

The Company does not have authorised capital or par value in respect of its issued shares.

## 22 Reserves and dividends

### (a) Reserves

#### Own credit spread reserve

This reserve represents the own credit spread component of the fair value movement for financial liabilities designated at fair value.

## Other capital reserve

This reserve represents the issuance of Tier 1 capital instruments. The Tier 1 capital instruments are perpetual subordinated loans on which coupon payments may be cancelled at the sole discretion of the Bank. The subordinated loans will be written down at the point of non-viability on the occurrence of a trigger event as defined by the Australian Prudential Regulation Authority ('APRA') or the Hong Kong Monetary Authority. They rank higher than ordinary shares in the event of a wind-up.

## Financial assets measured at FVOCI securities reserve

The FVOCI securities reserve includes the cumulative net change in the fair value of FVOCI investments until the investment is derecognised.

## Cash flow hedging reserve

The hedging reserve comprises the effective portion of the cumulative net change in the fair value of cash flow hedging instruments related to hedged transactions that have not been realised.

## Capital contribution reserve

This reserve represents the capital contribution received by the consolidated entity from the ultimate parent entity, HSBC Holdings plc, in respect of the various share-based payment schemes in operation.

## (b) Dividends

	2020		2019	
	Per share \$	Total \$m	Per share \$	Total \$m
<b>Ordinary shares</b>				
Dividend 1	0.095	65.0	0.097	66.5
Dividend 2	—	—	0.032	21.9
Dividend 3	—	—	0.048	32.8
Dividend 4	—	—	0.035	23.9
		65.0		145.1
<b>Tier 1 instruments</b>				
Dividend 1	—	7.4	—	8.8
Dividend 2	—	7.2	—	8.6
		14.6		17.4
		79.6		162.5

## 23 Commitments

	Consolidated		Company	
	2020 \$m	2019 \$m	2020 \$m	2019 \$m
Documentary credits and trade related transactions	124.4	110.7	124.4	110.7
Undrawn lending facilities	12,706.4	11,274.3	12,706.4	11,274.3
	12,830.8	11,385.0	12,830.8	11,385.0

## 24 Right-of-use assets

	Consolidated		Company	
	2020 \$m	2019 \$m	2020 \$m	2019 \$m
<b>Right-of-use assets</b>				
Balance at 1 Jan	267.9	241.1	267.9	241.1
New lease agreements	46.8	35.7	46.8	35.7
Decreases/amendments to leases	(30.2)	(8.9)	(30.2)	(8.9)
<b>Balance at 31 Dec</b>	<b>284.5</b>	<b>267.9</b>	<b>284.5</b>	<b>267.9</b>
<b>Leasehold office buildings accumulated depreciation</b>				
Balance at 1 Jan	(37.5)	—	(37.5)	—
Depreciation charge for the year	(39.4)	(37.5)	(39.4)	(37.5)
Decreases/amendments to leases	4.4	—	4.4	—
<b>Balance at 31 Dec</b>	<b>(72.5)</b>	<b>(37.5)</b>	<b>(72.5)</b>	<b>(37.5)</b>
<b>Carrying amounts</b>				
At 1 Jan	230.4	241.1	230.4	241.1
<b>At 31 Dec</b>	<b>212.0</b>	<b>230.4</b>	<b>212.0</b>	<b>230.4</b>

The expense related to short-term leases which have been directly expensed is \$2.6m (2019: \$4.1m) and the expenses related to variable leases is \$8.8m (2019: \$10.0m.)

## Lease liabilities

	Consolidated and Company	
	2020 \$m	2019 \$m
Current	34.8	34.7
Non-current	190.1	201.5
	224.9	236.2

The interest expense on the lease liabilities is \$9.2m (2019: \$7.4m) and is disclosed within the interest expense note 4. The total cash outflow for leases is \$32.1m (2019:\$33.8m) and is disclosed within the financing section in the statement of cash flows.

## 25 Contingent liabilities

	Consolidated		Company	
	2020 \$m	2019 \$m	2020 \$m	2019 \$m
Contingent liabilities in respect of guarantees given	834.4	1,046.2	834.4	1,046.2
Letters of credit and other contingencies	1,245.8	1,368.4	1,245.8	1,368.4

HSBC Bank Australia Limited and its controlled entities have commitments in respect of foreign exchange contracts, futures and options contracts, forward rate agreements, and currency and interest rate swap contracts. The commitments have been entered into in the normal course of business and it is not envisaged that any irrecoverable liability will arise from these contracts.

The Bank is party to legal proceedings and regulatory matters in a number of jurisdictions arising out of its normal business operations. Apart from the matters described below, the Bank considers that none of these matters are material. The recognition of provisions is determined in accordance with the accounting policies set out in note 3. While the outcome of legal proceedings and regulatory matters is inherently uncertain, management believes that, based on the information available to it, appropriate provisions have been made in respect of these matters as at 31 December 2020 in note 17. Where an individual provision is material, the fact that a provision has been made is stated and quantified, except to the extent doing so would be seriously prejudicial. Any provision recognised does not constitute an admission of wrongdoing or legal liability.

### Regulatory

In this environment of ongoing legislative reform, regulatory change and increased industry focus, financial institutions remain under considerable regulatory scrutiny, while the evolving regulatory landscape continues to present execution challenges. Regulators and other bodies such as ASIC, APRA, ACCC, AUSTRAC and the ATO continue to progress various investigations, reviews and inquiries (some of which are industry wide) that may involve the Bank. The nature of these can be wide-ranging. Across the industry, they currently include reviews and inquiries relating to governance, remuneration, culture, accountability and financial crime.

As a consequence of these investigations, reviews and inquiries and the Bank's ongoing program of internal investigations and reviews, actual or potential regulatory breaches from past conduct may be identified. At any point in time, there could be potential for a number of these matters to be under discussion with regulators. In December 2019, the Bank raised with AUSTRAC one such matter relating to the underreporting of a limited category of cross-border transactions involving Non-Bank Financial Institutions and other Financial Institutions. The Bank is continuing to work with AUSTRAC in relation to this matter in line with our open and transparent approach with regulators.

These regulators and other bodies may make findings that the Bank has engaged in misconduct, including breaches of law or conduct that falls below community standards and expectations. Any findings made may result in litigation, fines, penalties, revocation, suspension or variation of conditions of relevant regulatory licences or other enforcement or administrative action being taken by regulators or other bodies.

### Litigation

There are ongoing court proceedings, claims and possible claims for and against the Company. Contingent liabilities exist in respect of actual and potential claims and proceedings, including those listed below. An assessment of the Company's likely loss has been made on a case-by-case basis for the purpose of the financial statements but cannot always be reliably estimated. Where appropriate, specific provisions have been made in note 17.

In August 2016, HSBC Bank Australia Limited and other panel banks were named as defendants in two putative class actions filed in the New York District Court on behalf of persons who transacted in products related to the BBSW benchmark rates. The complaints allege, among other things, misconduct related to these benchmark rates in violation of US antitrust, commodities and racketeering laws, and state law. In the BBSW litigation, in November 2018, the court dismissed all foreign defendants including all the HSBC entities, on personal jurisdiction grounds. In April 2019, the plaintiff filed an amended complaint, which was dismissed in February 2020. The plaintiffs' right to appeal remains dormant.

There are many factors that may affect the range of outcomes, and the resulting financial impact, of these matters, which could be significant.

### Customer remediation

The Bank is currently undertaking a number of reviews to identify and resolve prior issues that have the potential to impact our customers. These reviews have identified, and may continue to identify, issues where the application of fees and charges may not have been applied consistently to certain cohorts of customers or in accordance with legal requirements. The Bank is remediating issues identified. An assessment of the Bank's likely loss has been made on a case-by-case basis for the purpose of the financial statements but cannot always be reliably estimated. Contingent liabilities may exist in respect of actual or potential claims, compensation payments and/or refunds identified as part of these reviews.

## 26 Fiduciary activities

	Consolidated	
	2020 \$m	2019 \$m
Funds under custody	531,309.9	533,012.2



The Bank provides custody and clearing services to global custodians, fund managers and broker dealers.

## 27 Additional financial instrument disclosures

### (a) Risk management

The HSBC Group formulates high-level risk management policies for the HSBC Group worldwide. The HSBC Group's risk management policies and procedures are subject to a high degree of oversight and guidance to ensure that all types of risk are systematically identified, measured, analysed and actively managed.

The following diagram and descriptions summarise key aspects of the risk management framework, including governance and structure, our risk management tools and our culture, which together help align employee behaviour with our risk appetite:

Key components of our risk management framework		
HSBC Values and risk culture		
Risk governance	Non-executive risk governance	The Board approves the Bank's risk appetite, plans and performance targets. It sets the 'tone from the top' and is advised by the Bank's Risk Committee.
	Executive risk governance	Our executive risk governance structure is responsible for the enterprise-wide management of all risks, including key policies and frameworks for the management of risk within the Group.
Roles and responsibilities	Three lines of defence model	Our 'three lines of defence' model defines roles and responsibilities for risk management. An independent Global Risk function helps ensure the necessary balance in risk/return decisions.
Processes and tools	Risk appetite	The Group has processes in place to identify/assess, monitor, manage and report risks to help ensure we remain within our risk appetite.
	Enterprise-wide risk management tools	
	Active risk management: identification/assessment, monitoring, management and reporting	
Internal controls	Policies and procedures	Policies and procedures define the minimum requirements for the controls required to manage our risks.
	Control activities	Operational and resilience risk management defines minimum standards and processes for managing operational risks and internal controls.
	Systems and infrastructure	The Group has systems and/or processes that support the identification, capture and exchange of information to support risk management activities.

The Risk Committee ('RC') is mandated by the Board to oversee the management of risk within the Bank and of the Bank's risk appetite and future risk strategy, including capital and liquidity management strategy. The executive Risk Management Meeting ('RMM') exercises oversight of the Bank's risk framework.

The RC has responsibility for oversight and advice to the Board on risk-related matters. The key responsibilities of the RC in this regard include providing advice to the Board on the overall risk appetite tolerance and strategy within the consolidated entity and seeking such assurance as it may deem appropriate that account has been taken of the current and prospective macroeconomic and financial environment. The RC is also responsible for the periodic review of the effectiveness of the internal control and risk management frameworks and advising the Board on all high level risk matters.

RMM has the responsibility for risk approval authorities and approving definitive risk-policies and controls. It monitors risk inherent to the financial services business, receives reports, determines action to be taken and reviews the efficacy of the risk management framework.

The Executive Committee and RMM are supported by a dedicated risk function headed by the Chief Risk Officer, who is a member of both the Executive Committee and RMM and at an entity level reports to the Chief Executive Officer.

#### Three lines of defence

To create a robust control environment to manage risks, we use an activity-based three lines of defence model. This model delineates management accountabilities and responsibilities for risk management and the control environment.

The model underpins our approach to risk management by clarifying responsibility and encouraging collaboration, as well as enabling efficient coordination of risk and control activities. The three lines of defence are summarised below:

- The first line of defence owns the risks and is responsible for identifying, recording, reporting and managing them in line with risk appetite, and ensuring that the right controls and assessments are in place to mitigate them.
- The second line of defence challenges the first line of defence on effective risk management, and provides advice and guidance in relation to the risk.
- The third line of defence is our Global Internal Audit function, which provides independent assurance that our risk management approach and processes are designed and operating effectively.

#### Material Banking Risks

The material risk types associated with our banking operations are described in the following table:

## Notes on the Consolidated Financial Statements

### Description of risks – banking operations

Risks	Arising from	Measurement, monitoring and management of risk
<b>Credit risk</b> Credit risk is the risk of financial loss if a customer or counterparty fails to meet an obligation under a contract.	Credit risk arises principally from direct lending, trade finance and leasing business, but also from other products such as guarantees and derivatives.	Credit risk is: <ul style="list-style-type: none"> <li>• measured as the amount that could be lost if a customer or counterparty fails to make repayments;</li> <li>• monitored using various internal risk management measures and within limits approved by individuals within a framework of delegated authorities; and</li> <li>• managed through a robust risk control framework, which outlines clear and consistent policies, principles and guidance for risk managers.</li> </ul>
<b>Treasury risk</b> Treasury risk is the risk of having insufficient capital, liquidity or funding resources to meet financial obligations and satisfy regulatory requirements, including the risk of adverse impact on earnings or capital due to structural foreign exchange exposures and changes in market interest rates.	Treasury risk arises from changes to the respective resources and risk profiles driven by customer behaviour, management decisions or the external environment.	Treasury risk is: <ul style="list-style-type: none"> <li>• measured through appetites set as target and minimum ratios;</li> <li>• monitored and projected against appetites and by using stress and scenario testing; and</li> <li>• managed through control of resources in conjunction with risk profiles and cash flows.</li> </ul>
<b>Market risk</b> Market risk is the risk that movements in market factors, such as foreign exchange rates, interest rates, credit spreads, equity prices and commodity prices, will reduce our income or the value of our portfolios.	Exposure to market risk is separated into two portfolios: trading portfolios and non-trading portfolios.	Market risk is: <ul style="list-style-type: none"> <li>• measured using sensitivities, value at risk and stress testing, giving a detailed picture of potential gains and losses for a range of market movements and scenarios, as well as tail risks over specified time horizons;</li> <li>• monitored using value at risk, stress testing and other measures, including the sensitivity of net interest income and the sensitivity of structural foreign exchange.</li> </ul>
<b>Resilience risk</b> Resilience risk is the risk that we are unable to provide critical services to our customers, affiliates and counterparties as a result of sustained and significant operational disruption.	Resilience risk arises from failures or inadequacies in processes, people, systems or external events.	Resilience risk is: <ul style="list-style-type: none"> <li>• measured using a range of metrics with defined maximum acceptable impact tolerances, and against our agreed risk appetite;</li> <li>• monitored through oversight of enterprise processes, risks, controls and strategic change programmes; and</li> <li>• managed by continual monitoring and thematic reviews.</li> </ul>
<b>Regulatory compliance risk</b> Regulatory compliance risk is the risk that we fail to observe the letter and spirit of all relevant laws, codes, rules, regulations and standards of good market practice, which as a consequence incur fines and penalties and suffer damage to our business.	Regulatory compliance risk arises from the risks associated with breaching our duty to our customers, inappropriate market conduct and breaching regulatory licensing, permission and rules.	Regulatory compliance risk is: <ul style="list-style-type: none"> <li>• measured by reference to risk appetite, identified metrics, incident assessments, regulatory feedback and the judgement and assessment of our regulatory compliance teams;</li> <li>• monitored against the first line of defence risk and control assessments, the results of the monitoring and control assurance activities of the second line of defence functions, and the results of internal and external audits and regulatory inspections; and</li> <li>• managed by establishing and communicating appropriate policies and procedures, training employees in them and monitoring activity to help ensure their observance. Proactive risk control and/or remediation work is undertaken where required.</li> </ul>
<b>Financial crime risk</b> Financial crime risk is the risk of knowingly or unknowingly helping parties to commit or to further illegal activity through HSBC, including money laundering, fraud, bribery and corruption, tax evasion, sanctions breaches, and terrorist and proliferation financing.	Financial crime risk arises from day-to-day banking operations.	Financial crime risk is: <ul style="list-style-type: none"> <li>• measured by reference to risk appetite, identified metrics, incident assessments, regulatory feedback and the judgement and assessment of our regulatory compliance teams</li> <li>• monitored against the first line of defence risk and control assessments, the results of the monitoring and control assurance activities of the second line of defence functions, and the results of internal and external audits and regulatory inspections; and</li> <li>• managed by establishing and communicating appropriate policies and procedures, training employees in them and monitoring activity to help ensure their observance. Proactive risk control and/or remediation work is undertaken where required</li> </ul>
<b>Model risk</b> Model risk is the potential for adverse consequences from business decisions informed by models, which can be exacerbated by errors in methodology, design or the way they are used.	Model risk arises in both financial and non-financial contexts whenever business decision making includes reliance on models.	Model risk is: <ul style="list-style-type: none"> <li>• measured by reference to model performance tracking and the output of detailed technical reviews, with key metrics including model review statuses and findings;</li> <li>• monitored against model risk appetite statements, insight from the independent review function, feedback from internal and external audits, and regulatory reviews; and</li> <li>• managed by creating and communicating appropriate policies, procedures and guidance, training colleagues in their application, and supervising their adoption to ensure operational effectiveness.</li> </ul>

For the following credit, liquidity risk and market risk management notes, the disclosures are for the consolidated entity as management monitors risk on a consolidated basis and because the market risk, credit risk and liquidity risk of the Bank are not considered materially different for separate disclosure. The exception is capital management where this is monitored for both the Company and consolidated entity.

## Risks related to COVID-19

The COVID-19 pandemic and its effect on the global economy has impacted our customers and our performance, and the future effects of the pandemic are uncertain. The outbreak necessitated governments to respond at unprecedented levels to protect public health, local economies and livelihoods. It has affected regions at different times and varying degrees. The varying government measures in response have added challenges, given the rapid pace of change and significant operational demands.

The speed at which countries and territories will be able to unwind their lockdown measures and return to pre-COVID-19 economic levels will vary based on the levels of infection and local political decisions and access and ability to rollout vaccines. There remains a risk of subsequent waves of infection.

The economic fallout from COVID-19 risks increasing inequality across markets that have already suffered from social unrest. This will leave the burden on governments and central banks to maintain or increase fiscal and monetary stimulus. After financial markets suffered a sharp fall in the early phases of the spread of COVID-19, they rebounded but still remain volatile. Depending on the degree to which global economic growth suffers permanent losses, financial asset prices may suffer further falls. Governments and central banks in major economies have deployed extensive measures to support their local populations. Measures implemented by governments have included income support to households and funding support to businesses.

RBA measures have included cuts to policy rates, support to funding markets and asset purchases. Central banks globally as well as in Australia are maintaining record low interest rates for a considerable period of time and the debt burden of governments is expected to rise significantly.

The Australian government's economic response helped business stability and kept Australians in jobs through the Job Keeper Payment and Boosting Cash Flow for Employers, and supported Australians in need with the Coronavirus Supplement and Early Release of Superannuation.

The Government's response is now transitioning to ensure the Australian economy recovers strongly by targeting additional temporary support measures to boost household incomes, bring forward business and infrastructure investment activity, and drive the unemployment rate back down. The Government is continuing to support those sectors, regions and communities that face significant challenges.

The Bank initiated market-specific measures to support our personal and business customers through these challenging times. These included mortgage assistance, payment holidays, the waiving of certain fees and charges, and liquidity relief for businesses facing market uncertainty and supply chain disruption.

For further details of our customer relief programmes refer to note 36.

As a result of COVID-19, business continuity responses have been successfully implemented and the majority of service level agreements have been maintained. The Bank has not experienced any major impacts to the supply chain from our third-party service providers due to COVID-19. The risk of damage or theft to our physical assets or criminal injury to our employees remains unchanged and no significant incidents have impacted our buildings or staff.

The significant changes in economic and market drivers, customer behaviours and government actions caused by COVID-19 have also impacted the performance of financial models. These include retail and wholesale credit models such as IFRS loss models, as well as capital models, traded risk models and models used in the asset/liability management process. This has required ongoing monitoring and frequent testing, particularly for credit models. It also has resulted in the use of compensating controls, specifically as overlays on top of model outputs to provide a more appropriate assessment.

By their nature, such compensating controls require a significant degree of management judgement and assumptions to be applied, and there is a risk that future performance may differ from such judgements and assumptions. The performance and usage of models over the 12 months will continue to be impacted by the consequences of the COVID-19 outbreak.

## (b) Credit risk disclosures

### Overview

Credit risk is the risk of financial loss if a customer or counterparty fails to meet a payment obligation under a contract. It arises principally from direct lending and trade finance business but also from certain other products such as guarantees and derivatives, and from the Bank's holding of debt and other securities.

### Credit Risk Management

#### Key Developments 2020

There were no material changes to the policies and practices for the management of credit risk in 2020. We continued to apply the requirements of AASB 9 'Financial Instruments' within Credit Risk.

Due to the unique market conditions in the COVID-19 outbreak, we expanded operational practices to provide short-term support to customers under the current policy framework.

#### Governance and Structure

We have established Group-wide credit risk management and related AASB 9 processes. We continue to assess the impact of economic developments in key markets on specific customers, customer segments or portfolios. As credit conditions change, we take mitigating action, including the revision of risk appetites or limits and tenors, as appropriate. In addition, we continue to evaluate the terms under which we provide credit facilities within the context of individual customer requirements, the quality of the relationship, local regulatory requirements, market practices and our local market position.

#### Credit risk sub-function

Credit approval authorities are delegated by the Board to the Chief Executive together with the authority to sub-delegate them. The Credit Risk sub-function in Global Risk is responsible for the key policies and processes for managing credit risk, which include formulating Group credit policies and risk rating frameworks, guiding the Bank's appetite for credit risk exposures, undertaking independent reviews and objective assessment of credit risk, and monitoring performance and management of portfolios.

## Notes on the Consolidated Financial Statements

The principal objectives of our credit risk management are:

- to maintain across HSBC a strong culture of responsible lending, and robust risk policies and control frameworks;
- to both partner and challenge our businesses in defining, implementing and continually re-evaluating our risk appetite under actual and scenario conditions; and
- to ensure there is independent, expert scrutiny of credit risks, their costs and their mitigation.

### Concentration of exposure

Concentrations of credit risk arise when a number of counterparties or exposures have comparable economic characteristics, or such counterparties are engaged in similar activities or operate in the same geographical areas or industry sectors so that their collective ability to meet contractual obligations is uniformly affected by changes in economic, political or other conditions. We use a number of controls and measures to minimise undue concentration of exposure in our portfolios across industries, countries and global businesses. These include portfolio and counterparty limits, approval and review controls, and stress testing.

### Credit quality of financial instruments

The five credit quality classifications each encompass a range of granular internal credit rating grades assigned to wholesale and retail lending businesses and the external ratings attributed by external agencies to debt securities, as shown in the table below. Under AASB 9 retail lending credit quality is disclosed based on a 12-month probability-weighted PD. The credit quality classifications for wholesale lending are unchanged and are based on internal credit risk ratings.

#### Credit quality classification

	Debt securities and other bills	Wholesale lending and derivatives		Retail lending	
	External credit rating	Internal credit rating	12-month probability of default %	Internal credit rating	12-month probability weighted PD %
<b>Quality classification</b>					
Strong	<b>A- and above</b>	<b>CRR0 to CRR2</b>	<b>0 – 0.169</b>	<b>Band 1 and 2</b>	<b>0.000-0.500</b>
Good	<b>BBB+ to BBB-</b>	<b>CRR3</b>	<b>0.170 – 0.740</b>	<b>Band 3</b>	<b>0.501-1.500</b>
Satisfactory	<b>BB+ to B and unrated</b>	<b>CRR4 to CRR5</b>	<b>0.741 – 4.914</b>	<b>Band 4 and 5</b>	<b>1.501-20.000</b>
Sub-standard	<b>B- to C</b>	<b>CRR6 to CRR8</b>	<b>4.915 – 99.999</b>	<b>Band 6</b>	<b>20.001-99.999</b>
Impaired	<b>Default</b>	<b>CRR9 to CRR10</b>	<b>100</b>	<b>Band 7</b>	<b>100.00</b>

#### Quality classification definitions

- 'Strong' exposures demonstrate a strong capacity to meet financial commitments, with negligible or low probability of default.
- 'Good' exposures demonstrate a good capacity to meet financial commitments, with low default risk.
- 'Satisfactory' exposures require closer monitoring and demonstrate an average to fair capacity to meet financial commitments, with moderate default risk.
- 'Sub-standard' exposures require varying degrees of special attention and default risk is of greater concern.
- 'Credit-impaired' exposures have been assessed as impaired.

### Summary of credit risk

The disclosure below presents the gross carrying/nominal amount of financial instruments to which the impairment requirements in AASB 9 are applied and the associated allowance for ECL. The following tables analyse loans by industry sector and represent the concentration of exposures on which credit risk is managed.

The table presents the maximum exposure to credit risk from on-balance sheet and off-balance sheet financial instruments, before taking account of any collateral held or other credit enhancements (unless such credit enhancements meet accounting offsetting requirements). For financial assets recognised on the Statement of financial position, the maximum exposure to credit risk equals their carrying amount, for financial guarantees and similar contracts granted, it is the maximum amount that would have to be paid if the guarantees were called upon. For loan commitments and other credit-related commitments that are irrevocable over the life of the respective facilities, it is generally the full amount of the committed facilities.

Summary of financial instruments to which the impairment requirements in AASB 9 are applied

	At 31 Dec 2020		At 31 Dec 2019	
	Gross carrying/ nominal amount \$m	Allowance for ECL \$m	Gross carrying/ nominal amount \$m	Allowance for ECL \$m
<b>Loans and advances to customers at amortised cost</b>				
Personal	27,050.4	(76.2)	25,186.0	(57.3)
– mortgages	26,272.2	(14.9)	24,199.2	(7.7)
– other personal (including credit cards)	778.2	(61.3)	986.8	(49.6)
Corporate and commercial	3,207.5	(68.9)	4,043.3	(67.0)
Non-bank financial institutions	118.1	(0.3)	156.3	(0.3)
Loans and advances to banks at amortised cost	14.9	–	25.5	–
Other financial assets measured at amortised cost	3,884.8	(0.6)	2,109.3	(0.1)
– cash and balances at central banks	3,342.6	–	1,633.1	–
– items in the course of collection from other banks	1.9	–	5.9	–
– reverse repurchase agreements – non-trading	–	–	–	–
– other financial assets held at amortised cost	540.3	(0.6)	470.3	(0.1)
<b>Total gross carrying amount on-balance sheet</b>	<b>34,275.7</b>	<b>(146.0)</b>	<b>31,520.4</b>	<b>(124.7)</b>
Loans and other credit related commitments	10,071.7	(6.5)	8,990.4	(5.2)
– personal	7,329.7	–	7,036.0	(0.1)
– corporate and commercial	2,015.0	(6.2)	1,444.2	(5.0)
– financial	727.0	(0.3)	510.2	(0.1)
Financial guarantee and similar contracts	791.6	(4.1)	1,012.9	(4.2)
– personal	8.4	–	12.5	(0.3)
– corporate and commercial	738.3	(4.1)	909.3	(3.8)
– financial	44.9	–	91.1	(0.1)
<b>Total nominal amount off-balance sheet</b>	<b>10,863.3</b>	<b>(10.6)</b>	<b>10,003.3</b>	<b>(9.4)</b>
<b>At 31 Dec 2020</b>	<b>45,139.0</b>	<b>(156.6)</b>	<b>41,523.7</b>	<b>(134.1)</b>
	Fair value	Memorandum allowance for ECL	Fair value	Memorandum allowance for ECL
	\$m	\$m	\$m	\$m
Debt instruments measured at FVOCI	12,056.3	(1.2)	11,479.8	(0.3)

## Notes on the Consolidated Financial Statements

The following table provides an overview of the consolidated entity's credit risk by stage and industry, and the associated ECL coverage. The financial assets recorded in each stage have the following characteristics:

- Stage 1: Unimpaired and without significant increase in credit risk on which a 12-month allowance for ECL is recognised.
- Stage 2: A significant increase in credit risk has been experienced since initial recognition on which a lifetime ECL is recognised.
- Stage 3: Objective evidence of impairment, and are therefore considered to be in default or otherwise credit impaired on which a lifetime ECL is recognised.

### Summary of credit risk (excluding debt instruments measured at FVOCI) by stage distribution and ECL sector

	Gross carrying/nominal amount				Allowance for ECL				ECL coverage %			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m	%	%	%	%
Loans and advances to customers at amortised cost	28,784.1	1,135.2	456.7	30,376.0	(34.8)	(30.5)	(80.0)	(145.3)	(0.1)	(2.7)	(17.5)	(0.5)
– personal	25,721.0	946.0	383.4	27,050.4	(29.4)	(28.7)	(18.1)	(76.2)	(0.1)	(3.0)	(4.7)	(0.3)
– corporate and commercial	2,945.0	189.2	73.3	3,207.5	(5.2)	(1.8)	(61.9)	(68.9)	(0.2)	(1.0)	(84.4)	(2.1)
– non-bank financial institutions	118.1	–	–	118.1	(0.2)	–	–	(0.2)	(0.2)	–	–	(0.2)
Loans and advances to banks at amortised cost	14.9	–	–	14.9	–	–	–	–	–	–	–	–
Other financial assets measured at amortised cost	3,875.3	2.0	7.4	3,884.7	0.1	–	(0.6)	(0.5)	–	–	(8.1)	–
Loans and other credit-related commitments	9,891.0	180.7	–	10,071.7	(4.0)	(2.6)	–	(6.6)	–	(1.4)	–	(0.1)
– personal	7,288.7	41.0	–	7,329.7	–	–	–	–	–	–	–	–
– corporate and commercial	1,875.3	139.7	–	2,015.0	(3.6)	(2.6)	–	(6.2)	(0.2)	(1.9)	–	(0.3)
– financial	727.0	–	–	727.0	(0.4)	–	–	(0.4)	(0.1)	–	–	(0.1)
Financial guarantee and similar contracts	613.0	177.3	4.1	794.4	(1.4)	(1.8)	(0.9)	(4.1)	(0.2)	(1.0)	(22.0)	(0.5)
– personal	7.3	–	0.8	8.1	–	–	–	–	–	–	–	–
– corporate and commercial	561.3	173.6	3.3	738.2	(1.3)	(1.8)	(0.9)	(4.0)	(0.2)	(1.0)	(27.3)	(0.5)
– financial	44.4	3.7	–	48.1	(0.1)	–	–	(0.1)	(0.2)	–	–	(0.2)
<b>At 31 Dec 2020</b>	<b>43,178.3</b>	<b>1,495.2</b>	<b>468.2</b>	<b>45,141.7</b>	<b>(40.1)</b>	<b>(34.9)</b>	<b>(81.5)</b>	<b>(156.5)</b>	<b>(0.1)</b>	<b>(2.3)</b>	<b>(17.4)</b>	<b>(0.3)</b>
Loans and advances to customers at amortised cost	27,113.2	2,074.6	197.8	29,385.6	(26.2)	(27.6)	(70.8)	(124.6)	(0.1)	(1.3)	(35.8)	(0.4)
– personal	23,141.4	1,905.0	139.6	25,186.0	(19.9)	(21.3)	(16.1)	(57.3)	(0.1)	(1.1)	(11.5)	(0.2)
– corporate and commercial	3,816.5	168.6	58.2	4,043.3	(6.0)	(6.3)	(54.7)	(67.0)	(0.2)	(3.7)	(94.0)	(1.7)
– non-bank financial institutions	155.3	1.0	–	156.3	(0.3)	–	–	(0.3)	(0.2)	–	–	(0.2)
Loans and advances to banks at amortised cost	25.4	0.1	–	25.5	–	–	–	–	–	–	–	–
Other financial assets measured at amortised cost	2,099.0	3.1	7.2	2,109.3	(0.1)	–	–	(0.1)	–	–	–	–
Loans and other credit-related commitments	8,914.2	68.2	8.0	8,990.4	(4.1)	(1.1)	–	(5.2)	–	(1.6)	–	(0.1)
– personal	6,995.8	32.2	8.0	7,036.0	–	(0.1)	–	(0.1)	–	(0.3)	–	–
– corporate and commercial	1,408.2	36.0	–	1,444.2	(4.0)	(1.0)	–	(5.0)	(0.3)	(2.8)	–	(0.3)
– financial	510.2	–	–	510.2	(0.1)	–	–	(0.1)	–	–	–	–
– Financial guarantee and similar contracts	880.9	129.0	3.0	1,012.9	(1.5)	(1.0)	(1.7)	(4.2)	(0.2)	(0.8)	(56.7)	(0.4)
– personal	12.2	–	0.3	12.5	–	–	(0.3)	(0.3)	–	–	(100.0)	(2.4)
– corporate and commercial	779.7	126.9	2.7	909.3	(1.4)	(1.0)	(1.4)	(3.8)	(0.2)	(0.8)	(51.9)	(0.4)
– financial	89.0	2.1	–	91.1	(0.1)	–	–	(0.1)	(0.1)	–	–	(0.1)
<b>At 31 Dec 2019</b>	<b>39,032.7</b>	<b>2,275.0</b>	<b>216.0</b>	<b>41,523.7</b>	<b>(31.9)</b>	<b>(29.7)</b>	<b>(72.5)</b>	<b>(134.1)</b>	<b>(0.1)</b>	<b>(1.3)</b>	<b>(33.6)</b>	<b>(0.3)</b>

Unless identified at an earlier stage, all financial assets are deemed to have suffered a significant increase in credit risk when they are 30 days past due and are transferred from stage 1 to stage 2. The disclosure below presents the ageing of stage 2 financial assets by those less than 30 and greater than 30 days past due and therefore presents those financial assets classified as stage 2 due to ageing (30 days past due) and those identified at an earlier stage (less than 30 days past due).

## Stage 2 and days past due analysis

	Gross carrying amount			Allowance for ECL			ECL coverage %		
	Of which:		Of which:	Of which:		Of which:	Of which:		Of which:
	Stage 2	1 to 29 DPD	30 and > DPD	Stage 2	1 to 29 DPD	30 and > DPD	Stage 2	1 to 29 DPD	30 and > DPD
	\$m	\$m	\$m	\$m	\$m	\$m	%	%	%
Loans and advances to customers at amortised cost	1,135.2	116.5	45.8	(30.5)	(0.3)	(1.2)	(2.7)	(0.3)	(2.6)
– personal	946.0	113.2	45.8	(28.7)	(0.3)	(1.2)	(3.0)	(0.3)	(2.6)
– corporate and commercial	189.2	3.3	–	(1.8)	–	–	(1.0)	–	–
– non-bank financial institutions	–	–	–	–	–	–	–	–	–
Loans and advances to banks at amortised cost	–	–	–	–	–	–	–	–	–
Other financial assets measured at amortised cost	2.0	0.1	0.7	–	–	–	–	–	–
Loan and other credit-related commitments	180.7	–	–	(2.6)	–	–	(1.4)	–	–
– personal	41.0	–	–	–	–	–	–	–	–
– corporate and commercial	139.7	–	–	(2.6)	–	–	(1.9)	–	–
– financial	–	–	–	–	–	–	–	–	–
Financial guarantee and similar contracts	177.3	–	–	(1.8)	–	–	(1.0)	–	–
– personal	–	–	–	–	–	–	–	–	–
– corporate and commercial	173.6	–	–	(1.8)	–	–	(1.0)	–	–
– financial	3.7	–	–	–	–	–	–	–	–
<b>At 31 Dec 2020</b>	<b>1,495.2</b>	<b>116.6</b>	<b>46.5</b>	<b>(34.9)</b>	<b>(0.3)</b>	<b>(1.2)</b>	<b>(2.3)</b>	<b>(0.3)</b>	<b>(2.6)</b>
Loans and advances to customers at amortised cost	2,074.6	193.5	66.7	(27.6)	(0.2)	(0.2)	(1.3)	(0.1)	(0.3)
– personal	1,905.0	193.5	49.8	(21.3)	(0.1)	(0.2)	(1.1)	(0.1)	(0.4)
– corporate and commercial	168.6	–	–	(6.3)	(0.1)	–	(3.7)	–	–
– non-bank financial institutions	1.0	–	16.9	–	–	–	–	–	–
Loans and advances to banks at amortised cost	0.1	–	–	–	–	–	–	–	–
Other financial assets measured at amortised cost	3.1	0.2	–	–	–	–	–	–	–
Loan and other credit-related commitments	68.2	–	–	(1.1)	–	–	(1.6)	–	–
– personal	32.2	–	–	(0.1)	–	–	(0.3)	–	–
– corporate and commercial	36.0	–	–	(1.0)	–	–	(2.8)	–	–
– financial	–	–	–	–	–	–	–	–	–
Financial guarantee and similar contracts	129.0	–	–	(1.0)	–	–	(0.8)	–	–
– personal	–	–	–	–	–	–	–	–	–
– corporate and commercial	126.9	–	–	(1.0)	–	–	(0.8)	–	–
– financial	2.1	–	–	–	–	–	–	–	–
<b>At 31 Dec 2019</b>	<b>2,275.0</b>	<b>193.7</b>	<b>66.7</b>	<b>(29.7)</b>	<b>(0.2)</b>	<b>(0.2)</b>	<b>(1.3)</b>	<b>(0.1)</b>	<b>(0.3)</b>

## Measurement uncertainty and sensitivity analysis of ECL

The recognition and measurement of ECL involves the use of significant judgement and estimation. We form multiple economic scenarios based on economic forecasts, apply these assumptions to credit risk models to estimate future credit losses, and probability-weight the results to determine an unbiased ECL estimate.

### Methodology

Four economic scenarios have been used to capture the exceptional nature of the current economic environment and to articulate management's view of the range of potential outcomes. Scenarios produced to calculate ECL are aligned to HSBC's Top and Emerging Risks. Three of these scenarios are drawn from consensus forecasts and distributional estimates. These include a central scenario, representing a most likely outcome, a downside and an upside scenario that represent meaningfully different outcomes from the central. The central scenario is created using the average of a panel of external forecasters ('the consensus') while consensus upside and downside scenarios are created with reference to distributions for select markets that capture forecasters views of the entire range of outcomes. Management have chosen to use a fourth scenario to represent their view of severe downside risks. The use of an additional scenario is in line with HSBC's Forward Economic Guidance (FEG) methodology and has been regularly used over the course of 2020. Management may include additional scenarios if they feel that the consensus scenarios do not adequately capture the Top and Emerging Risks. Unlike the consensus scenarios, these additional scenarios are driven by narrative assumptions, could be country-specific and may result in shocks that drive economic activity permanently away from trend.

### Description of Consensus Economic Scenarios

The economic assumptions presented in this section have been formed by HSBC with reference to external forecasts specifically for the purpose of calculating ECL.

The world economy experienced a deep economic shock in 2020. As COVID-19 spread globally, governments in many of our markets sought to limit the human impact by imposing significant restrictions on mobility, in turn driving the deep falls in activity that were observed in the first half of the year. Restrictions were eased as cases declined in response to the initial measures which in turn supported an initial rebound in economic activity by 3Q 2020. This increase in mobility unfortunately led to renewed transmission of the



## Notes on the Consolidated Financial Statements

virus in several countries, such that by year end, infection rates, hospitalisations and deaths had reached dangerously high levels, placing an enormous burden on health-care systems and leading governments to re-impose restrictions on mobility and causing economic activity to decline once more.

Economic forecasts are subject to a high degree of uncertainty in the current environment. Limitations of forecasts and economic models require a greater reliance on management judgement in addressing both the error inherent in economic forecasts and in assessing associated ECL outcomes. The scenarios used to calculate ECL in 2020 are described below.

### Consensus Central scenario

HSBC's Central scenario features an improvement in economic growth in 2021 as activity and employment gradually return to the levels experienced prior to the outbreak of COVID-19.

Despite the sharp contraction in activity, government fiscal support played a crucial role in averting significant financial distress. At the same time, the Reserve Bank of Australia implemented a variety of measures which included lowering its main policy interest rates, implementing emergency support measures for funding markets, and either restarting or increasing quantitative easing programs in order to support economies and the financial system. The Governments and Central Bank are expected to continue to work together to ensure that households and firms receive an appropriate level of financial support until restrictions on economic activity and mobility can be materially eased. Such support will ensure that labour and housing markets do not experience abrupt, negative corrections and will also limit the extent of long term structural damage to economies.

Our Central scenario incorporates expectations that governments and public health authorities will implement large vaccination programmes, first by inoculating critical groups and then increasing coverage to include the wider population. The deployment of mass vaccination programmes marks a significant step forward in combating the virus and will ease the burden on healthcare systems. We expect vaccination programs to contribute positively to recovery prospects and our Central scenario assumes a steady increase in the proportion of the population inoculated against COVID-19 over the course of 2021.

The key features of our Central scenario are:

- Growth in economic activity in 2021, supported by a successful rollout of vaccination programme coupled with effective non-pharmacological measures to contain the virus ('track and trace' systems and restrictions to mobility).
- Where fiscal support schemes are available, they will limit the increase in the unemployment rate in 2021. We expect a gradual reversion of the unemployment rate to pre-crisis levels over the course of the projection period as a result of economic recovery and due to the orderly withdrawal of fiscal support.
- Inflation will converge towards Central Bank targets.
- In advanced economies, fiscal support in 2020 led to large deficits and a significant increase in public debt. Fiscal support is expected to continue as needed and deficits are expected to reduce gradually over the projection period. Sovereign debt levels will remain high and our central scenario does not assume fiscal austerity.
- We expect Central Banks to remain prepared to provide further support as required.
- Policy interest rates will remain at current levels for an extended period and will increase very modestly towards the end of our projection period. Central Banks will continue to provide assistance through their asset purchase programmes as needed.

The following table describes the key macroeconomic variables and the probabilities assigned in the consensus Central Scenario.

#### Central scenario (Australian 5 year forecast average)

	2020	2019
	%	%
GDP growth rate	3.3	2.6
Inflation	2.0	2.3
Unemployment	6.1	5.0
House price growth	3.7	1.9
<b>Probability</b>	<b>70.0</b>	<b>80.0</b>

### Consensus Upside scenario

Compared to the consensus Central scenario, the consensus Upside scenario features a faster recovery in economic activity during the first two years, before converging to long-run trends.

The scenario is consistent with a number of key upside risk themes. These include the orderly and rapid global abatement of COVID-19 via successful containment and prompt deployment of a vaccine; de-escalation of tensions between the US and China; de-escalation of political tensions in Hong Kong; continued support from fiscal and monetary policy and smooth relations between the UK and the EU which enables the two parties to swiftly reach a comprehensive agreement on trade and services.

The following table describes key macroeconomic variables and the probabilities assigned in the consensus Upside scenario

#### Consensus Upside scenario (Australian 5 year forecast average)

	2020	2019
	%	%
GDP growth rate	3.9	3.3
Inflation	2.4	2.6
Unemployment	5.9	4.6
House price growth	4.6	3.2
<b>Probability</b>	<b>10.0</b>	<b>10.00</b>

### Consensus Downside scenario

2021 is expected to be a year of economic recovery, but the progression and management of the pandemic presents a key risk to global growth.



In the consensus Downside scenario, economic recovery is considerably weaker compared to the Central scenario. GDP growth remains weak, unemployment rates stay elevated and asset and commodity prices fall before gradually recovering.

The scenario is consistent with the key downside risks articulated above. Further outbreaks of COVID-19, coupled with delays in vaccination programmes lead to longer lasting restrictions on economic activity. Other global risks also increase and drive increased risk-aversion in asset markets.

The following table describes key macroeconomic variables and the probabilities assigned in the consensus Downside scenario:

#### Consensus Downside scenario (Australian 5 year forecast average)

	2020	2019
	%	%
GDP growth rate	2.1	1.0
Inflation	1.6	2.0
Unemployment	6.6	5.4
House price growth	2.5	0.7
<b>Probability</b>	<b>15.0</b>	<b>10.00</b>

#### Additional Downside scenario

An additional Downside scenario which features a global recession, has been created to reflect management's view of severe risks. Infections rise in 2021 and setbacks to vaccine programmes imply that successful roll out of vaccines only occurs towards the end of 2021 and it takes until the end of 2022 for the pandemic to come to an end. Governments and Central Banks are unable to significantly increase fiscal and monetary programmes which results in abrupt corrections in labour and asset markets.

The following table describes key macroeconomic variables and the probabilities assigned in the Additional Downside scenario:

#### Additional Downside scenario (Australian 5 year forecast average)

	2020	2019
	%	%
GDP growth rate	1.9	1.0
Inflation	1.1	2.0
Unemployment	8.5	5.4
House price growth	(1.0)	0.7
<b>Probability</b>	<b>5.0</b>	<b>–</b>

### Critical accounting estimates and judgements

The calculation of ECL under IFRS 9 involves significant judgements, assumptions and estimates. The level of estimation uncertainty and judgement has increased during 2020 as a result of the economic effects of the COVID-19 outbreak, including significant judgements relating to:

- the selection and weighting of economic scenarios, given rapidly changing economic conditions in an unprecedented manner, uncertainty as to the effect of government and central bank support measures designed to alleviate adverse economic impacts, and a wider distribution of economic forecasts than before the pandemic. The key judgements are the length of time over which the economic effects of the pandemic will occur, the speed and shape of recovery. The main factors include the effectiveness of pandemic containment measures, the pace of roll-out and effectiveness of vaccines, and the emergence of new variants of the virus, plus a range of geo-political uncertainties, which together represent a very high degree of estimation uncertainty, particularly in assessing downside scenarios;
- estimating the economic effects of those scenarios on ECL, where there is no observable historical trend that can be reflected in the models that will accurately represent the effects of the economic changes of the severity and speed brought about by the COVID-19 outbreak. Modelled assumptions and linkages between economic factors and credit losses may underestimate or overestimate ECL in these conditions, and there is significant uncertainty in the estimation of parameters such as collateral values and loss severity; and
- the identification of customers experiencing significant increases in credit risk and credit impairment, particularly where those customers have accepted payment deferrals and other reliefs designed to address short-term liquidity issues given muted default experience to date. The use of segmentation techniques for indicators of significant increases in credit risk involves significant estimation uncertainty.

#### How economic scenarios are reflected in the wholesale calculation of ECL

HSBC has developed a globally consistent methodology for the application of forward economic guidance into the calculation of ECL by incorporating forward economic guidance into the estimation of the term structure of PD and LGD. For PDs, HSBC considers the correlation of forward economic guidance to default rates for a particular industry in a country. For LGD calculations HSBC considers the correlation of forward economic guidance to collateral values and realisation rates for a particular country and industry. PDs and LGDs are estimated for the entire term structure of each instrument. For impaired loans, LGD estimates take into account independent recovery valuations provided by external consultants where available, or internal forecasts corresponding to anticipated economic conditions and individual company conditions. In estimating the ECL on impaired loans that are individually considered not to be significant, HSBC incorporates forward economic guidance proportionate to the probability-weighted outcome and the Central scenario outcome for non-stage 3 populations.

#### How economic scenarios are reflected in the retail calculation of ECL

HSBC has developed and implemented a globally consistent methodology for incorporating forecasts of economic conditions into ECL estimates. The impact of economic scenarios on PD is modelled at a portfolio level. Historical relationships between observed default rates and macroeconomic variables are integrated into IFRS 9 ECL estimates by leveraging economic response models. The impact of these scenarios on PD is modelled over a period equal to the remaining maturity of underlying asset or assets. The impact on LGD is modelled for mortgage portfolios by forecasting future loan-to-value ('LTV') profiles for the remaining maturity of the asset by leveraging national level forecasts of the house price index and applying the corresponding LGD expectation.

## Notes on the Consolidated Financial Statements

These models are based largely on historical observations and correlations with default rates. During 2020, management judgemental adjustments have been necessary to ensure that an appropriate amount of ECL impairment is recognised. The approaches to these adjustments are described below.

### Reflecting economic scenarios in ECL

The most severe projections at 31 December 2020 of macroeconomic variables are outside the historical observations on which IFRS 9 models have been built and calibrated to operate. Moreover, the complexities of governmental support programmes and regulatory guidance on treatment of customer impacts (such as forbearance and payment holidays) and the unpredictable pathways of the pandemic have never been modelled. Consequently, HSBC's AASB9 models, in some cases, generate outputs that appear overly sensitive when compared with other economic and credit metrics. Management judgemental adjustments are required to ensure that an appropriate amount of ECL impairment is recognised.

These data and model limitations have been addressed in the short term using in-model and post-model adjustments. This includes refining model inputs and outputs and using post-model adjustments based on management judgement and higher level quantitative analysis for impacts that are difficult to model. For the wholesale portfolio, this analysis produced a 'credit experts best estimate' to act as a benchmark against the modelled outcomes, and inform management judgemental adjustments. In the short term, the focus is on refining model inputs and outputs in a consistent and explainable manner, using management judgemental adjustments. Wider-ranging model changes will take time to develop and need more real data on which models can be trained.

### Reflecting economic scenarios in ECL

In the context of AASB 9, management judgemental adjustments are short-term increases or decreases to the ECL at either a customer or portfolio level to account for late breaking events, model deficiencies and expert credit judgement applied following management review and challenge.

We have internal governance in place to regularly monitor management judgemental adjustments and, where possible, to reduce the reliance on these through model recalibration or redevelopment, as appropriate. During 2020 the composition of modelled ECL and management judgemental adjustments changed significantly, reflecting the path of the pandemic, containment efforts and government support measures, and this is expected to continue to be the case until GDP growth resumes and the uncertainty over long-term unemployment abates.

At 31 December 2020, the only significant management judgemental adjustment is \$39.4m contained within the reported credit cards ECL in relation to data and model limitations resulting from the pandemic. This adjustment is applicable to the scenario-weighted ECL number. Adjustments in relation to Downside scenarios are more significant, as results are subject to greater uncertainty.

### Effect of multiple economic scenarios on ECL

The ECL recognised in the financial statements reflects the effect on expected credit losses of a range of possible outcomes, calculated on a probability-weighted basis, based on the economic scenarios described above, including management overlays where required. The probability-weighted amount is typically a higher number than would result from using only the Central (most likely) economic scenario. Expected losses typically have a non-linear relationship to the many factors which influence credit losses, such that more favourable macroeconomic factors do not reduce defaults as much as less favourable macroeconomic factors increase defaults.

### ECL based exposures at 31 Dec 2020

	Retail	Wholesale	Total
Central scenario	61.8	15.4	77.2
Upside scenario	56.6	11.4	68.0
Downside scenario	71.4	23.5	94.9
Additional downside scenario	229.7	44.0	273.7

### ECL based exposures at 31 Dec 2019

	Retail	Wholesale	Total
Central scenario	50.9	43.1	94.0
Upside scenario	43.3	26.6	69.9
Downside scenario	62.2	67.4	129.6

## Reconciliation of changes in gross carrying/nominal amount and allowances for loans and advances to banks and customers

The disclosure below provides a reconciliation of the consolidated entity's gross carrying/nominal amount and allowances for loans and advances to banks and customers including loan commitments and financial guarantees. The reconciliation excludes the movement in other financial assets measured at amortised cost and debt instruments measured at FVOCI. The 31 December 2020 gross carrying amount and allowance for ECL for these financial instruments is presented in the 'Summary of financial instruments to which the impairment requirements in AASB 9 are applied' disclosure.

Reconciliation of changes in gross carrying/nominal amount and allowances for loans and advances to customers including loan commitments and financial guarantees for retail clients

	Non-credit impaired				Credit impaired		Total	
	Stage 1		Stage 2		Stage 3			
	Gross carrying/ nominal amount	Allowance for ECL	Gross carrying/ nominal amount	Allowance for ECL	Gross carrying/ nominal amount	Allowance for ECL	Gross carrying/ nominal amount	Allowance for ECL
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
At 1 Jan 2020	30,149.4	(19.9)	1,937.2	(21.3)	147.9	(16.4)	32,234.5	(57.6)
Transfers of financial instruments:								
– Transfers from Stage 1 to Stage 2	(6,531.8)	17.1	6,531.8	(17.1)	–	–	–	–
– Transfers from Stage 2 to Stage 1	6,959.9	(37.4)	(6,959.9)	37.4	–	–	–	–
– Transfers to Stage 3	(252.7)	1.6	(198.1)	14.3	450.8	(15.9)	–	–
– Transfers from Stage 3	–	–	241.2	(4.0)	(241.2)	4.0	–	–
– Net remeasurement of ECL arising from transfer of stage	–	10.2	–	(13.1)	–	(0.2)	–	(3.1)
New financial assets originated or purchased	8,177.0	(7.1)	–	–	–	–	8,177.0	(7.1)
Changes to risk (model inputs) parameters and changes to ECL model	(1,927.0)	3.9	418.7	(28.8)	134.0	(20.5)	(1,374.3)	(45.4)
Asset derecognised (including final repayments)	(3,557.8)	2.2	(983.6)	3.8	(85.7)	9.5	(4,627.1)	15.5
Assets written off	–	–	–	–	(21.5)	21.5	(21.5)	21.5
Credit related modifications that resulted in derecognition	–	–	–	–	–	–	–	–
Others / Foreign exchange	–	–	–	–	–	–	–	–
At 31 Dec 2020	33,017.0	(29.4)	987.3	(28.8)	384.3	(18.0)	34,388.6	(76.2)
ECL release/(charge) for the period		(9.2)		38.1		11.2		40.1
Recoveries		–		–		(7.0)		(7.0)
Others		4.6		–		–		4.6
Total ECL charge for the period		(4.6)		38.1		4.2		37.7

Reconciliation of changes in gross carrying/nominal amount and allowances for loans and advances to customers including loan commitments and financial guarantees for wholesale clients

	Non-credit impaired				Credit impaired		Total	
	Stage 1		Stage 2		Stage 3			
	Gross carrying/ nominal amount	Allowance for ECL	Gross carrying/ nominal amount	Allowance for ECL	Gross carrying/ nominal amount	Allowance for ECL	Gross carrying/ nominal amount	Allowance for ECL
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
At 1 Jan 2020	6,758.9	(12.0)	334.6	(8.3)	60.9	(56.1)	7,154.4	(76.4)
Transfers of financial instruments:								
– Transfers from Stage 1 to Stage 2	(2,803.8)	8.4	2,803.8	(8.4)	–	–	–	–
– Transfers from Stage 2 to Stage 1	3,203.8	(13.1)	(3,203.8)	13.1	–	–	–	–
– Transfers to Stage 3	(11.1)	–	(64.4)	12.0	75.4	(12.0)	(0.1)	–
– Transfers from Stage 3	–	–	–	–	–	–	–	–
– Net remeasurement of ECL arising from transfer of stage	–	2.9	–	(6.2)	–	–	–	(3.3)
New financial assets originated or purchased	2,162.4	(3.6)	–	–	–	–	2,162.4	(3.6)
Changes to risk (model inputs) parameters and changes to ECL model	(2,116.0)	6.9	1,068.6	(8.2)	(29.5)	0.3	(1,076.9)	(1.0)
Asset derecognised (including final repayments)	(908.4)	0.2	(435.9)	0.2	(24.3)	0.5	(1,368.6)	0.9
Assets written off	–	–	–	–	(4.9)	4.9	(4.9)	4.9
Credit related modifications that resulted in derecognition	–	–	–	–	–	–	–	–
Others / Foreign exchange	–	–	–	–	(1.0)	(0.4)	(1.0)	(0.4)
At 31 Dec 2020	6,285.8	(10.3)	502.9	(5.8)	76.6	(62.8)	6,865.3	(78.9)
ECL release/(charge) for the period		(6.2)		14.5		(0.8)		7.5
Recoveries		–		–		–		–
Others		(0.7)		–		–		(0.7)
Total ECL charge for the period		(6.9)		14.5		(0.8)		6.8

## Notes on the Consolidated Financial Statements

### Reconciliation of changes in gross carrying/nominal amount and allowances for loans and advances to customers including loan commitments and financial guarantees for retail clients

	Non-credit impaired				Credit impaired		Total	
	Stage 1		Stage 2		Stage 3			
	Gross carrying/ nominal amount	Allowance for ECL	Gross carrying/ nominal amount	Allowancefor ECL	Gross carrying/ nominal amount	Allowancefor ECL	Gross carrying/ nominal amount	Allowance for ECL
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
At 1 Jan 2019	25,358.3	(26.9)	1,541.7	(25.7)	146.6	(34.4)	27,046.6	(87.0)
Transfers of financial instruments:								
– Transfers from Stage 1 to Stage 2	(1,841.7)	5.9	1,841.7	(5.9)	–	–	–	–
– Transfers from Stage 2 to Stage 1	1,239.9	(24.5)	(1,239.9)	24.5	–	–	–	–
– Transfers to Stage 3	(41.6)	0.2	(111.9)	16.5	153.5	(16.8)	–	(0.1)
– Transfers from Stage 3	–	–	28.8	(7.6)	(28.8)	7.6	–	–
– Net remeasurement of ECL arising from transfer of stage	–	10.6	–	(6.9)	–	(0.7)	–	3.0
New financial assets originated or purchased	8,265.2	(6.2)	–	–	–	–	8,265.2	(6.2)
Changes to risk (model inputs) parameters and changes to ECL model	(189.5)	19.6	110.3	(18.9)	(18.3)	(16.8)	(97.5)	(16.1)
Asset derecognised (including final repayments)	(2,641.2)	1.4	(233.4)	2.6	(64.3)	3.9	(2,938.9)	7.9
Assets written off	–	–	–	–	(40.8)	40.8	(40.8)	40.8
At 31 Dec 2019	30,149.4	(19.9)	1,937.3	(21.4)	147.9	(16.4)	32,234.6	(57.7)
ECL release/(charge) for the period		(25.4)		23.2		13.6		11.4
Recoveries		–		–		(5.7)		(5.7)
Others		0.1		–		–		0.1
Total ECL charge for the period		(25.3)		23.2		7.9		5.8

### Reconciliation of changes in gross carrying/nominal amount and allowances for loans and advances to customers including loan commitments and financial guarantees for wholesale clients

	Non-credit impaired				Credit impaired		Total	
	Stage 1		Stage 2		Stage 3			
	Gross carrying/ nominal amount  \$m	Allowance for ECL  \$m	Gross carrying/ nominal amount  \$m	Allowance for ECL  \$m	Gross carrying/ nominal amount  \$m	Allowance for ECL  \$m	Gross carrying/ nominal amount  \$m	Allowance for ECL  \$m
At 1 Jan 2019	6,820.5	(10.4)	974.6	(14.8)	86.4	(63.9)	7,881.5	(89.1)
Transfers of financial instruments:								
– Transfers from Stage 1 to Stage 2	(834.3)	1.1	834.3	(1.1)	–	–	–	–
– Transfers from Stage 2 to Stage 1	1,167.1	(8.7)	(1,167.1)	8.7	–	–	–	–
– Transfers to Stage 3	(4.4)	–	–	–	4.4	–	–	–
– Transfers from Stage 3	–	–	1.5	–	(1.5)	–	–	–
– Net remeasurement of ECL arising from transfer of stage	–	7.9	–	(0.7)	–	–	–	7.2
New financial assets originated or purchased	2,489.3	(12.2)	–	–	–	–	2,489.3	(12.2)
Changes to risk (model inputs) parameters and changes to ECL model	(2,098.0)	10.2	(159.5)	(0.1)	(4.2)	(0.4)	(2,261.7)	9.7
Changes to model used for ECL calculation								
Asset derecognised (including final repayments)	(781.3)	0.1	(149.2)	(0.3)	(24.4)	8.3	(954.9)	8.1
Others / Foreign exchange	–	–	–	–	0.2	(0.1)	0.2	(0.1)
At 31 Dec 2019	6,758.9	(12.0)	334.6	(8.3)	60.9	(56.1)	7,154.4	(76.4)
ECL release/(charge) for the period		(6.2)		1.1		(7.9)		(13.0)
Recoveries		–		–		–		–
Others		(0.6)		–		–		(0.6)
Total ECL charge for the period		(6.8)		1.1		(7.9)		(13.6)

Distribution of financial instruments to which the impairment requirements in AASB 9 are applied, by credit quality and stage allocation

	Gross carrying/notional amount						Allowance for ECL	Net
	Strong \$m	Good \$m	Satisfactory \$m	Sub- standard \$m	Credit impaired \$m	Total \$m		
Loans and advances to customers at amortised cost	23,630.6	4,151.1	1,724.9	412.6	456.7	30,375.9	(145.2)	30,230.7
– stage 1	23,605.1	4,079.8	1,094.1	5.1	–	28,784.1	(34.8)	28,749.3
– stage 2	25.5	71.3	630.8	407.5	–	1,135.1	(30.5)	1,104.6
– stage 3	–	–	–	–	456.7	456.7	(79.9)	376.8
– POCI	–	–	–	–	–	–	–	–
Loans and advances to banks at amortised cost	15.0	–	–	–	–	15.0	–	15.0
– stage 1	15.0	–	–	–	–	15.0	–	15.0
– stage 2	–	–	–	–	–	–	–	–
– stage 3	–	–	–	–	–	–	–	–
– POCI	–	–	–	–	–	–	–	–
Other financial assets measured at amortised cost	3,783.5	75.2	18.6	–	7.4	3,884.7	(0.5)	3,884.2
– stage 1	3,782.6	74.1	18.6	–	–	3,875.3	0.1	3,875.4
– stage 2	0.9	1.1	–	–	–	2.0	–	2.0
– stage 3	–	–	–	–	7.4	7.4	(0.6)	6.8
– POCI	–	–	–	–	–	–	–	–
Loan and other credit-related commitments	6,655.3	2,848.3	483.2	84.8	–	10,071.6	(6.4)	10,065.2
– stage 1	6,654.1	2,847.8	325.9	63.1	–	9,890.9	(3.8)	9,887.1
– stage 2	1.2	0.5	157.3	21.7	–	180.7	(2.6)	178.1
– stage 3	–	–	–	–	–	–	–	–
– POCI	–	–	–	–	–	–	–	–
Financial guarantees and similar contracts	223.2	241.3	299.3	22.7	4.7	791.2	(4.2)	787.0
– stage 1	210.8	205.1	196.1	–	–	612.0	(1.4)	610.6
– stage 2	12.4	36.2	103.2	22.7	–	174.5	(1.9)	172.6
– stage 3	–	–	–	–	4.7	4.7	(0.9)	3.8
– POCI	–	–	–	–	–	–	–	–
Debt instruments at FVOCI	12,055.2	–	–	–	–	12,055.2	(1.2)	12,054.0
– stage 1	12,055.2	–	–	–	–	12,055.2	(1.2)	12,054.0
– stage 2	–	–	–	–	–	–	–	–
– stage 3	–	–	–	–	–	–	–	–
– POCI	–	–	–	–	–	–	–	–
<b>At 31 Dec 2020</b>	<b>46,362.8</b>	<b>7,315.9</b>	<b>2,526.0</b>	<b>520.1</b>	<b>468.8</b>	<b>57,193.6</b>	<b>(157.5)</b>	<b>57,036.1</b>

## Notes on the Consolidated Financial Statements

### Distribution of financial instruments to which the impairment requirements in AASB 9 are applied, by credit quality and stage allocation (continued)

	Gross carrying/notional amount					Total \$m	Allowance for ECL \$m	Net \$m
	Strong \$m	Good \$m	Satisfactory \$m	Sub- standard \$m	Credit impaired \$m			
Loans and advances to customers at amortised cost	20,607.0	6,070.3	2,348.5	162.0	197.8	29,385.6	(124.6)	29,261.0
– stage 1	20,602.9	4,958.2	1,512.2	39.9	–	27,113.2	(26.2)	27,087.0
– stage 2	4.1	1,112.1	836.3	122.1	–	2,074.6	(27.6)	2,047.0
– stage 3	–	–	–	–	197.8	197.8	(70.8)	127.0
– POCI	–	–	–	–	–	–	–	–
Loans and advances to banks at amortised cost	25.5	–	–	–	–	25.5	–	25.5
– stage 1	25.4	–	–	–	–	25.4	–	25.4
– stage 2	0.1	–	–	–	–	0.1	–	0.1
– stage 3	–	–	–	–	–	–	–	–
– POCI	–	–	–	–	–	–	–	–
Other financial assets measured at amortised cost	1,996.0	78.3	27.8	–	7.2	2,109.3	(0.1)	2,109.2
– stage 1	1,993.7	77.5	27.8	–	–	2,099.0	(0.1)	2,098.9
– stage 2	2.3	0.8	–	–	–	3.1	–	3.1
– stage 3	–	–	–	–	7.2	7.2	–	7.2
– POCI	–	–	–	–	–	–	–	–
Loan and other credit-related commitments	5,745.6	2,867.4	341.5	27.9	8.0	8,990.4	(5.2)	8,985.2
– stage 1	5,745.6	2,866.7	301.9	–	–	8,914.2	(4.1)	8,910.1
– stage 2	–	0.7	39.6	27.9	–	68.2	(1.1)	67.1
– stage 3	–	–	–	–	8.0	8.0	–	8.0
– POCI	–	–	–	–	–	–	–	–
Financial guarantees and similar contracts	311.4	325.2	339.6	33.7	3.0	1,012.9	(4.2)	1,008.7
– stage 1	292.6	289.8	285.8	12.7	–	880.9	(1.5)	879.4
– stage 2	18.8	35.4	53.8	21.0	–	129.0	(1.0)	128.0
– stage 3	–	–	–	–	3.0	3.0	(1.7)	1.3
– POCI	–	–	–	–	–	–	–	–
Debt instruments at FVOCI	11,479.8	–	–	–	–	11,479.8	(0.3)	11,479.5
– stage 1	11,479.8	–	–	–	–	11,479.8	(0.3)	11,479.5
– stage 2	–	–	–	–	–	–	–	–
– stage 3	–	–	–	–	–	–	–	–
– POCI	–	–	–	–	–	–	–	–
At 31 Dec 2019	40,165.3	9,341.2	3,057.4	223.6	216.0	53,003.5	(134.4)	52,869.1

### Total retail lending by stage distribution

	Gross carrying amount				Allowance for ECL			
	Stage 1 \$m	Stage 2 \$m	Stage 3 \$m	Total \$m	Stage 1 \$m	Stage 2 \$m	Stage 3 \$m	Total \$m
By portfolio								
First lien residential mortgages	25,100.3	828.8	343.0	26,272.1	(3.8)	(4.1)	(7.0)	(14.9)
Other personal lending	620.7	117.2	40.3	778.2	(25.6)	(24.7)	(11.0)	(61.3)
– other	63.6	50.4	–	114.0	(2.0)	(0.7)	–	(2.7)
– credit cards	557.1	66.8	40.3	664.2	(23.6)	(24.0)	(11.0)	(58.6)
<b>At 31 Dec 2020</b>	<b>25,721.0</b>	<b>946.0</b>	<b>383.3</b>	<b>27,050.3</b>	<b>(29.4)</b>	<b>(28.8)</b>	<b>(18.0)</b>	<b>(76.2)</b>
By portfolio								
First lien residential mortgages	22,293.4	1,801.5	104.3	24,199.2	(1.2)	(1.4)	(5.1)	(7.7)
Other personal lending	848.0	103.5	35.3	986.8	(18.7)	(19.9)	(11.0)	(49.6)
– other	101.3	26.8	–	128.1	(2.1)	(0.6)	–	(2.7)
– credit cards	746.7	76.7	35.3	858.7	(16.6)	(19.3)	(11.0)	(46.9)
At 31 Dec 2019	23,141.4	1,905.0	139.6	25,186.0	(19.9)	(21.3)	(16.1)	(57.3)

### Total wholesale lending by stage distribution

	Gross carrying amount				Allowance for ECL			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Corporate and commercial	2,945.4	189.1	73.3	3,207.8	(5.1)	(1.7)	(61.9)	(68.7)
– agriculture, forestry and fishing	90.8	–	–	90.8	(0.1)	–	–	(0.1)
– mining and quarrying	139.7	19.0	–	158.7	(0.3)	(0.1)	–	(0.4)
– manufacture	354.1	9.5	–	363.6	(1.0)	(0.2)	–	(1.2)
– electricity, gas, steam and air-conditioning supply	64.8	–	–	64.8	(0.1)	–	–	(0.1)
– water supply, sewerage, waste management and remediation	3.5	–	–	3.5	–	–	–	–
– construction	11.6	–	–	11.6	(0.1)	–	–	(0.1)
– wholesale and retail trade, repair of motor vehicles and motorcycles	773.2	35.4	54.9	863.5	(1.1)	(0.5)	(45.8)	(47.4)
– transportation and storage	72.3	1.2	–	73.5	–	–	–	–
– accommodation and food	34.9	–	–	34.9	–	–	–	–
– publishing, audiovisual and broadcasting	214.9	0.2	–	215.1	–	–	–	–
– real estate	418.1	48.0	–	466.1	(0.7)	(0.1)	–	(0.8)
– professional, scientific and technical activities	487.7	5.5	–	493.2	(0.9)	–	–	(0.9)
– administrative and support services	87.8	63.4	–	151.2	(0.7)	(0.5)	–	(1.2)
– education	68.8	–	–	68.8	–	–	–	–
– arts, entertainment and recreation	14.8	6.9	–	21.7	(0.1)	(0.3)	–	(0.4)
– health and care	28.8	–	–	28.8	–	–	–	–
– other services	1.0	–	18.4	19.4	–	–	(16.1)	(16.1)
– activities of households	–	–	–	–	–	–	–	–
– government	78.6	–	–	78.6	–	–	–	–
Non-bank financial institutions	118.1	–	–	118.1	(0.2)	–	–	(0.2)
Loans and advances to banks	15.0	–	–	15.0	–	–	–	–
<b>At 31 Dec 2020</b>	<b>3,078.5</b>	<b>189.1</b>	<b>73.3</b>	<b>3,340.9</b>	<b>(5.3)</b>	<b>(1.7)</b>	<b>(61.9)</b>	<b>(68.9)</b>

### Total wholesale lending by stage distribution

	Gross carrying amount				Allowance for ECL			
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
	\$m	\$m	\$m	\$m	\$m	\$m	\$m	\$m
Corporate and commercial	3,816.5	168.6	58.2	4,043.3	(6.0)	(6.3)	(54.7)	(67.0)
– agriculture, forestry and fishing	11.7	–	–	11.7	–	–	–	–
– mining and quarrying	136.7	0.7	–	137.4	(0.3)	–	–	(0.3)
– manufacture	614.6	50.1	–	664.7	(2.0)	(1.1)	–	(3.1)
– construction	8.7	–	–	8.7	–	–	–	–
– wholesale and retail trade, repair of motor vehicles and motorcycles	1,304.5	43.6	37.9	1,386.0	(1.6)	(2.0)	(37.8)	(41.4)
– transportation and storage	78.4	–	–	78.4	–	–	–	–
– accommodation and food	38.4	–	–	38.4	–	–	–	–
– publishing, audiovisual and broadcasting	117.7	–	–	117.7	–	–	–	–
– real estate	554.0	31.8	–	585.8	(0.8)	(0.2)	–	(1.0)
– professional, scientific and technical activities	631.9	7.1	–	639.0	(0.9)	(0.4)	–	(1.3)
– administrative and support services	223.9	35.3	–	259.2	(0.3)	(2.6)	–	(2.9)
– education	10.0	–	–	10.0	–	–	–	–
– arts, entertainment and recreation	17.1	–	–	17.1	(0.1)	–	–	(0.1)
– health and care	61.5	–	–	61.5	–	–	–	–
– other services	2.6	–	20.3	22.9	–	–	(16.9)	(16.9)
– government	4.8	–	–	4.8	–	–	–	–
Non-bank financial institutions	155.3	1.0	–	156.3	(0.3)	–	–	(0.3)
Loans and advances to banks	25.4	0.1	–	25.5	–	–	–	–
<b>At 31 Dec 2019</b>	<b>3,997.2</b>	<b>169.7</b>	<b>58.2</b>	<b>4,225.1</b>	<b>(6.3)</b>	<b>(6.3)</b>	<b>(54.7)</b>	<b>(67.3)</b>

### Renegotiated loans and forbearance

The following table shows the gross carrying amounts of the Bank's holdings of renegotiated loans and advances to customers by industry sector and by stages. Wholesale renegotiated loans are classified as stage 3 until there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows, observed over a minimum one-year period, and there are no other indicators of impairment. Personal renegotiated loans are deemed to remain credit impaired until repayment or derecognition.



## Notes on the Consolidated Financial Statements

### Renegotiated loans and advances to customers at amortised cost by stage distribution

	Stage 1 \$m	Stage 2 \$m	Stage 3 \$m	Total \$m
<b>Gross carrying amount</b>				
Personal				
– first lien residential mortgages	–	–	70.4	70.4
– other personal lending	–	–	22.7	22.7
Wholesale				
– corporate and commercial	–	–	38.0	38.0
– non-bank financial institutions	–	–	–	–
<b>At 31 Dec 2020</b>	–	–	131.1	131.1
<b>Allowance for ECL</b>				
Personal				
– first lien residential mortgages	–	–	(1.5)	(1.5)
– other personal lending	–	–	(7.9)	(7.9)
Wholesale				
– corporate and commercial	–	–	(37.3)	(37.3)
– non-bank financial institutions	–	–	–	–
<b>At 31 Dec 2020</b>	–	–	(46.7)	(46.7)
Gross carrying amount				
Personal				
– first lien residential mortgages	–	–	47.2	47.2
– other personal lending	–	–	7.7	7.7
Wholesale				
– corporate and commercial	–	–	38.0	38.0
– non-bank financial institutions	–	–	–	–
<b>At 31 Dec 2019</b>	–	–	92.9	92.9
<b>Allowance for ECL</b>				
Personal				
– first lien residential mortgages	–	–	(2.2)	(2.2)
– other personal lending	–	–	(4.1)	(4.1)
Wholesale				
– corporate and commercial	–	–	(37.8)	(37.8)
– non-bank financial institutions	–	–	–	–
<b>At 31 Dec 2019</b>	–	–	(44.1)	(44.1)

### Collateral and other credit enhancements loans and advances

Although collateral can be an important mitigant of credit risk, it is HSBC Group's practice to lend on the basis of the customer's ability to meet their obligations out of their cash flow resources rather than rely on the value of security offered. Depending on the customer's standing and the type of product, facilities may be provided unsecured. However, for other lending a charge over collateral is obtained and considered in determining the credit decision and pricing. In the event of default the Bank may use the collateral as a source of repayment.

Depending on its form, collateral can have a significant financial effect in mitigating the Bank's exposure to credit risk.

The Bank may also manage its risk by employing other types of collateral and credit risk enhancements, such as second charges, other liens and unsupported guarantees, but the valuation of such mitigants is less certain and their financial effect has not been quantified.

The collateral types are as follows:

- in the personal sector, mortgages over residential properties (mortgage loans where the loan has a greater than 80% loan to value, the level at which lender mortgage insurance is required on origination, represent 5.2% (2019: 7.9%) of total mortgage loan portfolio);
- in the commercial and industrial sector, charges over business assets such as premises, stock and debtors;
- in the commercial real estate sector, charges over the properties being financed and personal guarantees; and
- in the financial sector, charges over financial instruments such as debt securities and equities in support of trading facilities.

Collateral held on impaired assets as at 31 December 2020 was \$343.3m (2019: \$109.3m).

### Derivatives

The International Swaps and Derivatives Association ('ISDA') Master Agreement is the Bank's preferred agreement for documenting derivatives activity. It provides the contractual framework within which dealing activity across a full range of over the counter products is conducted, and contractually binds both parties to apply close-out netting across all outstanding transactions covered by an agreement if either party defaults or another pre-agreed termination event occurs. It is common, and the Bank's preferred practice, for the parties to execute a Credit Support Annex ('CSA') in conjunction with the ISDA Master Agreement. Under a CSA, collateral is passed between the parties to mitigate the counterparty risk inherent in outstanding positions. The majority of the Bank's CSAs are with financial institution clients.

## Other credit risk exposures

In addition to collateralised lending described above, other credit enhancements are employed and methods used to mitigate credit risk arising from financial assets. These are described in more detail below.

Government, bank and other financial institution issued securities may benefit from additional credit enhancement, notably through government guarantees that reference these assets. Corporate issued debt securities are primarily unsecured. Debt securities issued by banks and financial institutions include asset-backed securities ('ABSs') and similar instruments, which are supported by underlying pools of financial assets.

## Concentration of exposure

Concentrations of credit risk exist when a number of counterparties are engaged in similar activities, or operate in the same geographical areas or industry sectors and have similar economic characteristics so that their ability to meet contractual obligations is similarly affected by changes in economic, political or other conditions.

## (c) Treasury risk disclosures

### Capital

The Bank's approach to capital management is driven by its strategic and organisational requirements, taking into account the regulatory, economic and commercial environment in which it operates.

It is the Bank's objective to maintain a strong capital base to support the development of its business and to meet regulatory capital requirements at all times.

There is an annual Bank capital plan which is approved by the Board. The plan is drawn up with the objective of maintaining both an appropriate amount of capital and an optimal mix between the different components of capital. In accordance with HSBC Group's Capital Management Framework, capital generated in excess of planned requirements is returned to the shareholder, normally by way of dividends.

The principal forms of capital are included in the following balances on the consolidated Statement of financial position: share capital, retained earnings, other reserves, and subordinated liabilities. Capital also includes the general reserve for credit losses.

### Externally imposed capital requirements

The Bank is an Authorised Deposit Taking Institution and is subject to APRA regulation under the authority of the Banking Act 1959.

The local regulator sets and monitors the Bank and consolidated entity's capital requirements under a tiered approach to the measurement of the entity's capital adequacy covering:

- Level 1 – Bank; and
- Level 2 – consists of the consolidated Bank, excluding non-controlled subsidiaries and subsidiaries with non-financial operations and securitisation special purpose vehicles.

The Bank uses the standardised approach to credit risk, operational risk and market risk.

During the year, the Bank and the consolidated entity complied with all of the externally imposed capital requirements by APRA.

### Basel III

The Prudential Standards issued by APRA are generally consistent with the guidelines developed by the Basel Committee on Banking Supervision (BCBS). The BCBS guidelines are known as Basel III and provide for national discretion in certain areas. APRA began consultations on revisions to the capital framework for authorised deposit-taking institutions (ADIs) to implement "unquestionably strong" capital ratios and the Basel III reforms in February 2018. APRA proposes to implement the Basel III reforms with the internationally agreed date of 1 January 2023, except for the operational risk requirements for ADIs using an advanced measurement approach that will be implemented on 1 January 2021. On the basis that the proposed changes by APRA are under consultation and subject to national discretion it is not possible to determine the impact on the Bank.

## Liquidity and Funding

Liquidity risk is the risk that the consolidated entity does not have sufficient financial resources to meet its obligations as they fall due or will have to do so at an excessive cost. This risk arises from mismatches in the timing of cash flows. Funding risk (a form of liquidity risk) arises when the liquidity needed to fund illiquid asset positions cannot be obtained at the expected terms and/or when required.

The objective of the consolidated entity's liquidity and funding management framework is to ensure that all foreseeable funding commitments can be met when due, and that access to the wholesale markets is coordinated and cost-effective. To this end, the consolidated entity maintains a diversified funding base comprising core retail and corporate customer deposits and institutional balances. This is complemented with a portfolio of highly liquid assets diversified by maturity which are held to enable the Bank to respond quickly and smoothly to unforeseen liquidity requirements.

The Board is responsible for determining the liquidity risk appetite for the Bank and ensuring that there is an appropriate organisation structure for managing this risk. Under authorities delegated by the Board, the Asset and Liability Committee ('ALCO') is responsible for managing all Asset, Liability and Capital Management ('ALCM') issues including liquidity and funding risk management.

Compliance with liquidity and funding requirements is monitored by HSBC Bank Australia ALCO who also report to the HSBC Holdings plc ALCO on a regular basis. This process includes:

- maintaining compliance with relevant regulatory requirements of the HSBC Bank Australia;
- monitoring liquidity and funding ratios against internal and regulatory requirements;
- managing term funding profile where appropriate;
- maintaining debt financing plans where appropriate;
- monitoring of depositor concentration in order to avoid undue reliance on large individual depositors and ensuring a satisfactory overall funding mix; and

## Notes on the Consolidated Financial Statements

- maintaining liquidity and funding contingency plans. These plans identify early indicators of stress conditions and describe actions to be taken in the event of difficulties arising from systemic or other crises, while minimising adverse long-term implications for the business.

### Term Funding Facility ('TFF')

On 19 March 2020, the Reserve Bank announced extensive measures aimed at providing liquidity to financial markets and to support the banks in providing credit to businesses. As well as lowering the cash rate, these measures included injecting extra liquidity into the financial system through daily market operations, the purchasing of Australian Government bonds in the secondary market, increasing the interest rate on Exchange Settlement Account Balances, and the introduction of the TFF. The RBA extended the TFF on 1 September 2020. The TFF makes funding available to banks at a fixed interest rate of 10 basis points, for a maximum of three years. To access the TFF, banks must pledge eligible collateral, which includes self-securitised residential mortgage-backed securities. The Bank has utilised \$739.0m of its total TFF facility at 31 December 2020.

### Liquidity coverage ratio ('LCR')

The LCR metric is designed to promote the short-term resilience of a bank's liquidity profile. It aims to ensure that a bank has sufficient unencumbered high-quality liquid assets ('HQLA') to meet its liquidity needs in a 30-calendar-day liquidity stress scenario. HQLA consist of cash or assets that can be converted into cash at little or no loss of value in markets. The Bank manages to both APRA and HSBC Group European Banking Authority based LCR models.

### Net stable funding ratio ('NSFR')

The NSFR requires institutions to maintain sufficient stable funding relative to required stable funding, and reflects a bank's long-term funding profile (funding with a term of more than a year). It is designed to complement the LCR. The Bank manages to both APRA and HSBC Group European Banking Authority-based NSFR models.

### Cash flows payable by the consolidated entity under financial liabilities by remaining contractual maturities

	On demand \$m	Due within 3 months \$m	Due between 3 and 12 months \$m	Due between 1 and 5 years \$m	Due after 5 years \$m	Total \$m
Deposits by banks	2,959.1	—	—	—	—	2,959.1
Customer accounts	33,051.9	1,715.3	1,804.8	8.8	—	36,580.9
Repurchase agreements – non-trading	—	—	—	744.1	1,308.3	2,052.4
Financial liabilities designated at fair value	—	—	—	44.1	—	44.1
Derivatives	248.9	—	9.1	59.9	42.9	360.8
Debt securities in issue	32.3	59.2	231.0	620.6	245.2	1,188.3
Subordinated liabilities (related parties)	—	—	—	—	516.6	516.6
Other financial liabilities	700.6	21.0	29.3	133.5	65.9	950.3
<b>Statement of financial position</b>	<b>36,992.7</b>	<b>1,795.5</b>	<b>2,074.2</b>	<b>1,610.9</b>	<b>2,179.0</b>	<b>44,652.4</b>
Loan and other credit-related commitments	12,830.8	—	—	—	—	12,830.8
Financial guarantees and similar contracts	806.5	—	—	—	—	806.5
<b>At 31 Dec 2020</b>	<b>50,630.0</b>	<b>1,795.5</b>	<b>2,074.2</b>	<b>1,610.9</b>	<b>2,179.0</b>	<b>58,289.7</b>
Deposits by banks	1,787.1	1,276.0	—	—	—	3,063.1
Customer accounts	28,117.7	3,661.2	682.1	9.4	—	32,470.4
Repurchase agreements – non-trading	—	4,068.7	—	—	—	4,068.7
Financial liabilities designated at fair value	—	—	—	46.1	—	46.1
Derivatives	0.2	3.2	8.3	39.1	21.6	72.4
Debt securities in issue	—	100.4	—	—	—	100.4
Subordinated liabilities (related parties)	—	—	—	—	462.7	462.7
Other financial liabilities	526.8	128.6	30.4	132.1	151.8	969.7
Statement of financial position	30,431.8	7,763.3	720.8	226.7	2,110.9	41,253.5
Loan and other credit-related commitments	11,385.0	—	—	—	—	11,385.0
Financial guarantees and similar contracts	1,027.3	—	—	—	—	1,027.3
<b>At 31 Dec 2019</b>	<b>42,844.1</b>	<b>7,763.3</b>	<b>720.8</b>	<b>226.7</b>	<b>2,110.9</b>	<b>53,665.8</b>

\* Financial guarantees are recognised in the earliest period in which payment is due from the entity.

The balances in the above table will not agree directly to the balances in the consolidated Statement of financial position as the table incorporates all cash flows, on an undiscounted basis, related to both principal as well as those associated with all future coupon payments. Liabilities in trading portfolios have not been analysed by contractual maturity because trading assets and liabilities are typically held for short periods of time.

Cash flows payable in respect of customer accounts are primarily contractually repayable on demand or at short notice. In practice, however, short-term deposit balances remain stable as inflows and outflows broadly match and a significant portion of loan commitments and guarantee contracts expire without being drawn upon. The Bank's approach to managing liquidity risk is set out above.

### (d) Market risk disclosures

Market risk is the risk that movements in foreign exchange rates, interest rates, credit spreads, or equity and commodity prices will result in profits or losses to the Bank. Market risk arises on financial instruments which are measured at fair value and those which are measured at amortised cost. The objective of market risk management is to control market risk exposures to achieve an optimal return while maintaining risk at acceptable levels.

The Bank monitors market risk separately for trading portfolios and non-trading portfolios. Trading portfolios include positions arising from market-making in exchange rate and interest rate as well as in debt securities. Trading risks arise either from customer-related business or from market-making proprietary position-taking.

The management of market risk is principally undertaken in Global Markets through risk limits approved by the HSBC Group's Executive Committee. Wholesale and Market Risk, a unit within the Risk function, develops risk management policies and measurement techniques.

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. Limits are set using a combination of risk measurement techniques, including position limits, sensitivity limits, as well as value at risk 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.

### Value at risk ('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 (99% for the Bank). The use of VaR is integrated in the risk management of market risk in the Bank and VaR is calculated for all trading-intent positions regardless of how those exposures are capitalised. Where there is not an approved internal model, the appropriate local rules to capitalise exposures are used. The Bank's models are based predominantly on historical simulation. VaR is calculated at a 99% confidence level for a one-day holding period. Although a valuable guide to risk, VaR should always be viewed in the context of its limitations. For example:

- 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 use of a holding period assumes that all positions can be liquidated or the risk offset during that period. This may not fully reflect the market risk arising at times of severe illiquidity, when the holding period may be insufficient to liquidate or hedge all positions fully;
- the use of a 99% confidence level, by definition, does not take into account losses that might occur beyond this level of confidence;
- VaR is calculated on the basis of exposures outstanding at the close of business and therefore does not necessarily reflect intra-day exposures; and
- VaR is unlikely to reflect loss potential on exposures that only arise under significant market movements.

The Bank 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 Bank's stress testing regime provides senior management with an assessment of the impact of extreme events on the market risk exposures of the Bank.

### Total and trading VaR for the consolidated entity

	Total VaR		Trading VaR	
	2020 \$m	2019 \$m	2020 \$m	2019 \$m
Average	7.5	6.0	0.1	0.2
Maximum	11.8	9.0	0.8	1.3
Minimum	3.1	2.9	—	—
<b>At 31 Dec</b>	<b>7.0</b>	<b>8.7</b>	<b>0.4</b>	<b>0.2</b>

Total VaR at 31 December 2020 was \$7.0m which decreased from the VaR of \$8.7m observed as at 31 December 2019 though average was higher. The higher average VaR was due to re-deployment of maturities in the balance sheet management books and higher volatility observed in the year 2020.

Total Trading VaR at 31 December 2020 increased to \$0.4m (2019: \$0.2m) although the average was lower due to lower risk being run by the relevant trading desks.

### Trading assets and liabilities

The Bank's trading assets and liabilities are in substantially all cases originated by Global Banking and Markets ('GB&M'). As described in note 3(g), the assets and liabilities are classified as held for trading if they have been acquired or incurred principally for the purpose of selling or repurchasing in the near term, or form part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent pattern of short-term profit-taking. These assets and liabilities are treated as traded risk for the purposes of market risk management, other than a limited number of exceptions, primarily in Global Banking ('GB') where the short-term acquisition and disposal of the assets are linked to other non-trading-related activities such as loan origination.

### Financial liabilities designated at fair value

Financial liabilities designated at fair value are primarily fixed-rate securities issued for funding purposes. As described in note 3(h), an accounting mismatch would arise if the debt securities were accounted for at amortised cost because the derivatives which economically hedge market risks on the securities would be accounted for at fair value with changes recognised in the Income statement. The market risks of these liabilities are treated as non-traded risk, the principal risks being interest rate and/or foreign exchange risks.

### Derivative assets and liabilities

As described in note 9 the Bank undertakes derivative activity for three primary purposes; to create risk management solutions for clients, to manage the portfolio risks arising from client business and to manage and hedge the Bank's own risks. Most of the Bank's derivative exposures arise from sales and trading activities within GB&M and are treated as traded risk for market risk management purposes. Within derivative assets and liabilities there are portfolios of derivatives which are not risk managed on a trading intent basis and are treated as non-traded risk for VaR measurement purposes. These arise when the derivative was entered into in order to manage risk arising from non-traded exposures. These include non-qualifying hedging derivatives, and derivatives qualifying for fair value and cash flow hedge accounting. The use of non-qualifying hedges whose primary risks relate to interest rate and foreign exchange exposure is described in note 3(l). Details of derivatives in fair value and cash flow hedge accounting relationships are given in note 9 to the Financial Statements. The Bank's primary risks in respect of these instruments relate to interest rate and foreign exchange risks.

## Notes on the Consolidated Financial Statements

### Loans and advances to customers

The primary risk on assets within loans and advances to customers is the credit risk of the borrower. The risk of these assets is treated as non-trading risk for market risk management purposes.

### Financial assets measured at FVOCI

Financial assets measured at FVOCI include assets held on an available-for-sale basis. An analysis of the Bank's holdings of these securities by accounting classification and issuer type is shown in note 10. The majority of these securities are mainly held within Balance Sheet Management in GB&M. The positions which are originated in order to manage structural interest rate and liquidity risk are treated as non-trading risk for the purposes of market risk management.

### Trading

The Bank's control of market risk is based on restricting individual operations to trading within a list of permissible instruments authorised for each site by Wholesale and Market Risk, and enforcing rigorous new product approval procedures. In particular, trading in the more complex derivative products is concentrated in offices with appropriate levels of product expertise and robust control systems.

In addition, at both portfolio and position levels, market risk in trading portfolios is monitored and controlled using a complementary set of techniques such as VaR and present value of a basis point, together with stress and sensitivity testing and concentration limits. These techniques quantify the impact on capital of defined market movements.

### Non-trading portfolios

Market risk in non-trading portfolios arises principally from mismatches between the future yield on assets and their funding cost as a result of interest rate changes. Analysis of this risk is complicated by having to make assumptions on embedded optionality within certain investment product areas, such as the incidence of mortgage prepayments, and from behavioural assumptions regarding the economic duration of liabilities which are contractually repayable on demand such as current accounts, and the repricing behaviour of managed rate products.

In order to manage this risk optimally, market risk in non-trading portfolios is transferred to Global Markets or to separate books managed under the supervision of the Bank ALCO. The transfer of market risk to books managed by Global Markets or supervised by the Bank's ALCO is usually achieved by a series of internal deals between the business units and these books. When the behavioural characteristics of a product differ from its contractual characteristics, the behavioural characteristics are assessed to determine the true underlying interest rate risk. Bank ALCOs regularly monitor all such behavioural assumptions and interest rate risk positions, to ensure they comply with interest rate risk limits established by senior management.

As noted above, in certain cases, the non-linear characteristics of products cannot be adequately captured by the risk transfer process. For example, both the flow from customer deposit accounts to alternative investment products and the precise prepayment speeds of mortgages will vary at different interest rate levels. In such circumstances, simulation modelling is used to identify the impact of varying scenarios on valuations and net interest income.

Once market risk has been consolidated in Global Markets or ALCO-managed books, the net exposure is typically managed through the use of interest rate swaps within agreed limits.

The Bank also monitors the sensitivity of projected net interest income under varying interest rate scenarios. The Bank aims, through its management of market risk in non-trading portfolios, to mitigate the impact of prospective interest rate movements which could reduce future net interest income, while balancing the cost of such hedging activities on the current net revenue stream.

A large part of the Bank's exposure to changes in net interest income arising from movements in interest rates relates to its core deposit franchise. The Bank's core deposit franchise is exposed to changes in the value of the deposits raised and spreads against wholesale funds. The value of core deposits increases as interest rates rise and decreases as interest rates fall. This risk is, however, asymmetrical in a very low interest rate environment as there is limited room to lower deposit pricing in the event of interest rate reductions.

## 28 Fair values of financial instruments carried at fair value

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

Financial instruments measured at fair value on an ongoing basis include trading assets and liabilities, instruments designated at fair value, derivatives, and financial investments classified as financial assets measured at FVOCI (including treasury and other eligible bills, debt securities and equity securities).

### Control framework

Fair values are subject to a control framework designed to ensure that they are either determined, or validated, by a function independent of the risk-taker.

For all financial instruments where fair values are determined by reference to externally quoted prices or observable pricing inputs to models, independent price determination or validation is utilised. In inactive markets, direct observation of a traded price may not be possible. In these circumstances, the Bank will source alternative market information to validate the financial instrument's fair value, with greater weight given to information that is considered to be more relevant and reliable.

For fair values determined using valuation models, the control framework may include, as applicable, development or validation by independent support functions of:

- the logic within valuation models;
- the inputs to those models;
- any adjustments required outside the valuation models; and
- where possible, model outputs.

Valuation models are subject to a process of due diligence and calibration before becoming operational and are calibrated against external market data on an on-going basis. Changes in fair value are generally subject to a profit and loss analysis process. This process disaggregates changes in fair value into three high level categories:

- portfolio changes, such as new transactions or maturing transactions;
- market movements, such as changes in foreign exchange rates or equity prices; and
- other movement, such as changes in fair value adjustments.

To this end, the ultimate responsibility for the determination of fair values lies within the Finance function, which reports to the Chief Financial Officer, who establishes the accounting policies and procedures governing valuation, and is responsible for ensuring that these comply with all relevant accounting standards.

#### **Determination of fair value of financial instruments carried at fair value**

Fair values are determined according to the following hierarchy:

- Level 1 – Valuation technique using quoted market price: Financial instruments with quoted prices for identical instruments in active markets that the Bank can access at the measurement date;
- Level 2 – Valuation technique using observable inputs: Financial instruments with quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in inactive markets and financial instruments valued using models where all significant inputs are observable; and
- Level 3 – Valuation technique with significant unobservable inputs: Financial instruments valued using valuation techniques where one or more significant inputs are unobservable.

The judgement as to whether a market is active may include, but is not restricted to, the consideration of factors such as the magnitude and frequency of trading activity, the availability of prices and the size of bid/offer spreads. The bid/offer spread represents the difference in prices at which a market participant would be willing to buy compared with the price at which they would be willing to sell. In inactive markets, obtaining assurance that the transaction price provides evidence of fair value or determining the adjustments to transaction prices that are necessary to measure the fair value of the instrument requires additional work during the valuation process.

The best evidence of fair value is a quoted price in an actively traded market. In the event that the market for a financial instrument is not active, a valuation technique is used.

The majority of valuation techniques employ only observable market data, and so the reliability of the fair value measurement is high. However, certain financial instruments are valued on the basis of valuation techniques that feature one or more significant market inputs that are not observable. For these instruments, the fair value derived is more judgemental.

‘Not observable’ in this context means that there is little or no current market data available from which to determine the level at which an arm’s length transaction would likely occur, but it generally does not mean that there is absolutely no market data available upon which to base a determination of fair value (historical data may, for example, be used). Furthermore, the assessment of hierarchy level is based on the lowest level of input that is significant to the fair value of the financial instrument. Consequently, the level of uncertainty in the determination of the unobservable inputs will generally give rise to valuation uncertainty that is less than the fair value itself.

The valuation models used where quoted market prices are not available incorporate certain assumptions that the HSBC Group anticipates would be used by a market participant to establish fair value. Where the HSBC Group anticipates that there are additional considerations not included within the valuation model, adjustments may be adopted outside the model. Examples of such adjustments are:

- credit risk adjustment: an adjustment to reflect the creditworthiness of the over-the-counter derivatives counterparties; and
- market data/model uncertainty: an adjustment to reflect uncertainties in fair values based on uncertain market data inputs (e.g. as a result of illiquidity) or in areas where the choice of valuation model is particularly subjective.

Transaction costs are not included in the fair value calculation. Trade origination costs such as brokerage, fee expenses and post-trade costs are included in operating expenses. The future cost of administering the over-the-counter derivative portfolio is also not included in fair value, but is expensed as incurred.

A detailed description of the valuation techniques applied to instruments of particular interest follows:

- debt securities, treasury and eligible bills (level 1, level 2): These instruments are valued based on quoted market prices from an exchange, dealer, broker, industry group or pricing service, where available. When they are unavailable, the fair value is determined by reference to quoted market prices for similar instruments, adjusted as appropriate for the specific circumstances of the instruments;
- derivatives (level 2): over-the-counter (i.e. non-exchange traded) derivatives are valued using valuation models. Valuation models calculate the present value of expected future cash flows, based upon ‘no-arbitrage’ principles. For many vanilla derivatives products, such as interest rate swap and European options, the modelling approaches used are standard across the industry. Examples of inputs that are generally observable include foreign exchange spot and forward rates, benchmark interest rate curves and volatility surfaces for commonly traded option products. Examples of inputs that may be unobservable include volatility surfaces, in whole or in part, for less commonly traded option products, and correlations between market factors; and
- debt securities on issue (level 2): designated at fair value: In certain circumstances, the Bank applies the fair value option to own debt in issue. Where available, the fair value will be based upon quoted prices in an active market for the specific instrument concerned. Where not available, the fair value will be based upon an Own Issuance Curve constructed from HSBC Bank Australia Limited’s funding grid as well as the credit gradient grid which is based on Credit Default Swap Spreads for HSBC Holdings plc. The fair value of the instruments therefore includes the effect of own credit spread. Movements taken into reserves arising from changes in the credit spread of liabilities issued by the Bank reverse over the contractual life of the debt.

## Notes on the Consolidated Financial Statements

### Financial instruments carried at fair value (consolidated)

	Valuation Techniques				Amount with HSBC*	Total
	Level 1 \$m	Level 2 \$m	Level 3 \$m	Total Third Party \$m		
At 31 Dec 2020						
Assets						
Derivatives	0.2	81.7	—	81.9	97.1	179.0
Financial assets measured at FVOCI	7,914.1	4,142.3	4.4	12,060.8	—	12,060.8
Liabilities						
Financial liabilities designated at fair value	—	43.2	—	43.2	—	43.2
Derivatives	—	93.7	—	93.7	266.1	359.8
At 31 Dec 2019						
Assets						
Derivatives	—	34.7	—	34.7	39.8	74.5
Financial assets measured at FVOCI	7,241.8	4,238.0	4.0	11,483.8	—	11,483.8
Liabilities						
Financial liabilities designated at fair value	—	43.7	—	43.7	—	43.7
Derivatives	—	33.2	—	33.2	127.0	160.2

\* Transactions with HSBC are predominantly instruments based on observable inputs. As described below the risk associated instruments with significant unobservable inputs are all backed out to other HSBC entities and all reside within level 2.

Aside from the assets and liabilities outlined in the table above, the carrying values are a reasonable approximation of fair values. The movement between level 1 and level 2 was \$169.7m (2019: \$503.5m) and Nil (2019: \$153.0m) between level 2 and level 1.

## 29 Notes to the Statements of cash flows

### Reconciliation of profit for the year to net cash from / (used) in operating activities

	Consolidated		Company	
	2020 \$m	2019 \$m	2020 \$m	2019 \$m
<b>Profit for the year</b>	<b>220.3</b>	330.4	<b>220.3</b>	330.4
Depreciation and amortisation	54.1	49.4	54.1	49.4
(Increase)/decrease in interest receivable	4.8	(4.3)	4.8	(4.3)
Increase/(decrease) in interest payable	3.2	(10.7)	3.2	(10.7)
Loan impairment charges	46.2	(7.3)	46.2	(7.3)
(Profit)/loss on the sale of investments	(27.2)	(37.1)	(27.2)	(37.1)
Provision for impairment of financial investments	0.8	—	0.8	—
Increase/(decrease) in provisions	5.3	(0.2)	5.3	(0.2)
Increase/(decrease) in provision for employee entitlements	6.1	0.8	6.1	0.8
Increase/(decrease) in intercompany payable account	(29.4)	—	(29.4)	—
(Increase)/decrease in sundry debtors	5.4	2.3	(0.7)	2.5
Increase/(decrease) in sundry creditors	(42.7)	(171.6)	(36.4)	(172.7)
<b>Changes in operating assets and liabilities</b>				
Net (increase)/decrease in trading assets	95.5	105.4	95.5	105.4
Cash inflows/(outflows) from movements in other assets/liabilities	(101.7)	(7.3)	(102.7)	(6.4)
Net (increase)/decrease in loans and bills advanced	(1,069.7)	(3,535.8)	(1,069.5)	(3,535.8)
Net increase in deposits and other borrowings	2,116.6	5,829.8	3,010.1	5,829.8
<b>Net cash from operating activities</b>	<b>1,287.6</b>	2,543.8	<b>2,180.5</b>	2,543.8

Cash and cash equivalents at the end of the financial year as shown in the Statements of cash flows are reconciled to the related items in the Statements of financial position as follows:

### Reconciliation of cash and cash equivalents

	Consolidated		Company	
	2020 \$m	2019 \$m	2020 \$m	2019 \$m
Cash and balances at central banks	3,342.6	1,633.1	3,342.6	1,633.1
Placings with banks with remaining maturity 3 months or less	14.9	25.5	14.9	25.5
Securities purchased from related entities under agreements to resell	—	—	—	—
<b>Total cash and cash equivalents</b>	<b>3,357.5</b>	1,658.6	<b>3,357.5</b>	1,658.6

## Financing facilities

At 31 December 2020 and 31 December 2019 there are no committed facilities.



### 30 Assets pledged as security for liabilities and collateral accepted as security for assets

	Consolidated		Company	
	2020 \$m	2019 \$m	2020 \$m	2019 \$m
Financial assets pledged as collateral	3,532.9	2,565.2	3,532.9	2,565.2
Fair value of the collateral permitted to sell or repledge in the absence of default	—	—	—	—
Fair value of collateral actually sold or repledged	—	—	—	—

These transactions are conducted under terms that are usual and customary to collateralised transactions, including, where relevant, standard repurchase agreements.

The amount of assets pledged to secure liabilities may be greater than the book value of assets utilised as collateral. For example, in the case of securitisations and covered bonds, the amount of liabilities issued plus mandatory over-collateralisation is less than the book value of the pool of assets available for use as collateral. This is also the case where assets are placed with a custodian or a settlement agent which has a floating charge over all the assets placed to secure any liabilities under settlement accounts.

These transactions are conducted under terms that are usual and customary to collateralised transactions including, where relevant, standard securities lending and borrowing, repurchase agreements and derivative margining. The Bank places both cash and non-cash collateral in relation to derivative transactions.

### 31 Securitisations and other structured transactions

The consolidated entity enters into transactions from time to time by which it transfers recognised financial assets directly to third parties or to special purpose entities. These transfers may give rise to the full or partial derecognition of the financial assets concerned.

Full derecognition occurs when the consolidated entity transfers its contractual right to receive cash flows from the financial assets, or retains the right but assumes an obligation to pass on the cash flows from the assets, and transfers substantially all the risks and rewards of ownership. The risks include credit, interest rate, currency, prepayment and other price risks.

Partial derecognition occurs when the Bank sells or otherwise transfers financial assets in such a way that some but not substantially all of the risks and rewards of ownership are transferred but control is retained. These financial assets are recognised on the Statement of financial position to the extent of the Bank's continuing involvement.

#### Carrying amount of the assets not derecognised and their associated liabilities

		Consolidated		Company	
		2020	2019	2020	2019
	Notes	\$m	\$m	\$m	\$m
<b>Carrying amount of asset</b>					
Loans and advances to customers	*	3,559.2	1,855.9	3,559.2	1,855.9
<b>Total</b>		<b>3,559.2</b>	<b>1,855.9</b>	<b>3,559.2</b>	<b>1,855.9</b>
<b>Carrying amount of related liability</b>					
Sale and repurchase agreement		2,046.8	1,457.5	2,046.8	1,457.5
Related party liability		—	—	892.9	—
Debt securities on issue		892.9	—	—	—
<b>Total</b>		<b>2,939.7</b>	<b>1,457.5</b>	<b>2,939.7</b>	<b>1,457.5</b>

\* The Bank has performed mortgage loan securitisations, whereby it has sold mortgage loans to the Lion Series 2009-1 and Lion 2020 Trust who have funded purchases through the issue of securities to the Bank and external investors respectively. The Bank provides swaps and services (including servicing and trust management) to the Trust on an arm's length basis in accordance with the APRA Prudential Guidelines (APS120 'Securitisation') and is entitled to the residual income from the notes. In addition the Bank provides a liquidity facility to the Lion Series 2009-1 Trust.

## 32 Maturity analysis of assets, liabilities and off-balance sheet commitments

### Maturity analysis of assets, liabilities and off-balance sheet commitments

	Due not more than 1 month \$m	Due within 3 months \$m	Due between 3 and 12 months \$m	Due between 1 and 5 years \$m	Due after 5 years \$m	Total \$m
<b>Financial assets</b>						
Cash and balances at central banks	3,342.6	—	—	—	—	3,342.6
Items in the course of collection from other banks	1.9	—	—	—	—	1.9
Other financial assets mandatorily measured through profit or loss	4.4	—	—	—	—	4.4
Derivatives	178.7	—	—	—	—	178.7
Loans and advances to banks	85.0	—	—	—	—	85.0
Loans and advances to customers	1,931.3	872.4	1,024.3	3,904.9	22,499.3	30,232.2
Financial assets measured through other comprehensive income	255.8	400.0	5,525.1	4,959.7	920.1	12,060.7
Accrued income and other financial assets	628.4	21.7	20.8	0.1	—	671.0
<b>Total financial assets at 31 Dec 2020</b>	<b>6,428.1</b>	<b>1,294.1</b>	<b>6,570.2</b>	<b>8,864.7</b>	<b>23,419.4</b>	<b>46,576.5</b>
Non-financial assets	—	—	—	—	459.8	459.8
<b>Total assets at 31 Dec 2020</b>	<b>6,428.1</b>	<b>1,294.1</b>	<b>6,570.2</b>	<b>8,864.7</b>	<b>23,879.2</b>	<b>47,036.3</b>
<b>Financial liabilities</b>						
Deposits by banks	2,959.1	—	—	—	—	2,959.1
Customer accounts	33,022.3	1,711.4	1,786.7	4.0	—	36,524.4
Repurchase agreements – non-trading	1,308.3	—	—	738.6	—	2,046.9
Items in the course of transmission to other banks	45.1	—	—	—	—	45.1
Financial liabilities designated at fair value	—	—	—	43.2	—	43.2
Derivatives	248.9	—	8.9	59.5	42.6	359.9
Debt securities in issue	24.2	44.5	173.6	466.3	184.3	892.9
Accruals and other financial liabilities	432.1	12.8	12.6	1.2	0.3	459.0
Lease liabilities	3.1	6.3	25.4	123.5	66.6	224.9
Subordinated liabilities	—	—	—	—	350.0	350.0
<b>Total financial liabilities at 31 Dec 2020</b>	<b>38,043.1</b>	<b>1,775.0</b>	<b>2,007.2</b>	<b>1,436.3</b>	<b>643.8</b>	<b>43,905.4</b>
Non-financial liabilities	—	—	—	—	266.5	266.5
<b>Total liabilities at 31 Dec 2020</b>	<b>38,043.1</b>	<b>1,775.0</b>	<b>2,007.2</b>	<b>1,436.3</b>	<b>910.3</b>	<b>44,171.9</b>
<b>Off-balance sheet commitments given</b>						
Loan and other credit-related commitments	12,823.9	—	—	—	—	12,823.9

Financial assets						
Cash and balances at central banks	1,633.1	—	—	—	—	1,633.1
Items in the course of collection from other banks	5.9	—	—	—	—	5.9
Other financial assets mandatorily measured through profit or loss	4.2	—	—	—	—	4.2
Derivatives	72.3	—	0.6	1.7	—	74.6
Loans and advances to banks	85.4	—	—	—	—	85.4
Loans and advances to customers	2,471.5	778.8	1,123.2	3,872.4	21,014.8	29,260.7
Reverse repurchase agreements – non-trading	—	—	—	—	—	—
Financial assets measured through other comprehensive income	359.9	1,562.7	3,867.0	4,669.1	1,025.2	11,483.9
Accrued income and other financial assets	498.5	27.9	24.8	0.1	—	551.3
<b>Total financial assets at 31 Dec 2019</b>	<b>5,130.8</b>	<b>2,369.4</b>	<b>5,015.6</b>	<b>8,543.3</b>	<b>22,040.0</b>	<b>43,099.1</b>
Non financial assets	—	—	—	—	473.9	473.9
<b>Total assets at 31 Dec 2019</b>	<b>5,130.8</b>	<b>2,369.4</b>	<b>5,015.6</b>	<b>8,543.3</b>	<b>22,513.9</b>	<b>43,573.0</b>
Financial liabilities	1,787.1	1,271.0	—	—	—	3,058.1
Deposits by banks	29,919.6	1,852.8	676.1	6.7	—	32,455.2
Customer accounts	4,022.7	—	—	—	—	4,022.7
Repurchase agreements – non-trading	60.2	—	—	—	—	60.2
Items in the course of transmission to other banks	—	—	—	—	—	—
Trading liabilities	—	—	—	43.7	—	43.7
Financial liabilities designated at fair value	91.4	3.2	6.1	38.5	20.9	160.1
Derivatives	—	100.0	—	—	—	100.0
Debt securities in issue	333.1	13.1	2.6	0.7	—	349.5
Accruals and other financial liabilities	2.9	5.8	26.1	119.5	81.9	236.2
Subordinated liabilities	—	—	—	—	250.0	250.0
<b>Total financial liabilities at 31 Dec 2019</b>	<b>36,050.4</b>	<b>3,245.9</b>	<b>710.9</b>	<b>209.1</b>	<b>519.4</b>	<b>40,735.7</b>
Non financial liabilities	—	—	—	—	293.9	293.9
<b>Total liabilities at 31 Dec 2019</b>	<b>36,050.4</b>	<b>3,245.9</b>	<b>710.9</b>	<b>209.1</b>	<b>813.3</b>	<b>41,029.6</b>
Off-balance sheet commitments given						
Loan and other credit-related commitments	11,363.6	—	—	—	—	11,363.6

### 33 Related party disclosures

#### Controlling entities

The ultimate chief entity of the HSBC Group is HSBC Holdings plc, a company incorporated in England and Wales. The immediate parent entity in Australia is HSBC Australia Holdings Pty Ltd.

#### Ownership interest in related parties

Interests held in related parties are set out in note 12.

#### Amounts receivable from or payable to related parties

	Consolidated		Company	
	2020	2019	2020	2019
	\$	\$	\$	\$
<b>Aggregate amounts receivable</b>				
Other related entities	200,408,000	147,579,462	200,169,707	147,579,462
<b>Aggregate amounts payable</b>				
Owing to parent in respect of tax	(7,448,536)	11,660,589	(7,448,536)	11,660,589
Other related entities	2,837,416,706	5,045,637,535	3,730,864,603	5,045,637,535
Subordinated liabilities – other related entities	350,000,000	250,000,000	350,000,000	250,000,000
	3,179,968,170	5,307,298,124	4,073,416,067	5,307,298,124

#### Aggregate of amounts received or receivable from or paid or payable to related parties during the year

	Consolidated		Company	
	2020	2019	2020	2019
	\$	\$	\$	\$
<b>Interest revenue</b>				
Other related entities	1,403,110	5,663,423	1,403,110	5,663,423
Key management personnel	252,941	173,506	252,941	173,506
<b>Interest expense</b>				
Other related entities	27,641,644	73,012,845	30,667,522	73,012,845
<b>Management fees paid</b>				
Other related entities	185,469,979	157,737,694	185,469,979	157,737,694
<b>Management fees received</b>				
Other related entities	145,955,511	149,457,754	145,955,511	149,457,754
<b>Fee income</b>				
Other related entities	10,663,659	12,261,139	10,663,659	12,261,139
<b>Fee expense</b>				
Other related entities	17,487,650	13,232,614	17,487,650	13,232,614
<b>Employee benefits</b>				
Share based payments	8,828,853	7,283,124	8,828,853	7,283,124
<b>Dividend paid</b>				
Controlling entity	79,374,895	162,528,623	79,624,210	162,528,623

#### Transactions with related parties

All transactions with related parties during the financial year were conducted on normal commercial terms and conditions.

Various related entities were counterparties in respect of certain foreign exchange contracts, swap contracts and forward rate agreements undertaken by the consolidated entity. All such contracts are undertaken at arm's length under normal commercial terms and conditions.

Loans and lease receivables outstanding as at balance date included \$1,230,926,467 (Consolidated) (2019: \$1,246,611,660), which were guaranteed by The Hongkong and Shanghai Banking Corporation Limited and other related corporations under normal commercial terms and conditions.

Management accounting and administrative services were provided by the Company to certain related entities free of charge within the HSBC Group. Otherwise these services are charged on a time and cost basis.

## Notes on the Consolidated Financial Statements

### 34 Key management personnel disclosures

The following were key management personnel of the consolidated entity at any time during the reporting period and unless otherwise indicated were key management personnel for the entire period:

<b>Executive Directors</b>		
Noel McNamara	Interim Chief Executive Officer	Resigned 29 February 2020
Kaber Mclean	Chief Executive Officer	Appointed 1 March 2020
<b>Non-executive Directors</b>		
Graham Bradley	Chairman	Resigned 21 October 2020
Carol Austin		
Grant King	Chairman	Appointed Chairman 22 October 2020
Matthew Lobner		
Kenneth Ng		
Jann Skinner		
Geoff Wilson		
<b>Company Secretary</b>		
Robert Agati		
<b>Executives</b>		
Gunalan Bhaskaran	Head of Regulatory Compliance & Interim Chief Risk Officer	Resigned as CRO 1 March 2020, Stepped down from Exco 1 Oct 2020, Resigned 18 Nov 2020.
Guy Dickinson	Head of Global Markets	
Sarah Duncan	Head of Financial Crime Compliance	Resigned 30 Sep 2020
Emma Hider	Chief Financial Officer	Resigned 31 Oct 2020
Steve Hughes	Head of Commercial Banking	
Brenton Hush	Chief Operating Officer	
Hamish Kelly	Head of Global Banking	
David Matthews	Head of Communications	Resigned 4 May 2020
Noel McNamara	Chief Risk Officer	Returned to CRO role 1 March 2020
Rani Mina	Chief Compliance Officer (CCO)	Resigned General Counsel, Appointed CCO 1 Oct 2020
Maria S W Lu	Interim General Counsel	Appointed 1 Oct 2020
Paul Murphy	Head of Human Resources	
Jessica Power	Head of Wealth & Personal Banking	Title change from Head of RBWM
Justin Holloway	Chief Financial Officer	Appointed 1 Nov 2020
Tala Booker	Head of Communications	Appointed 1 Sep 2020
Alison Kahler	Interim Head of Communications	Appointed 04 May 2020 to 31 Aug 2020

The key management personnel compensation included in 'employee compensation and benefits' note 6 are as follows.

#### Transactions with key management personnel

	Consolidated		Company	
	2020	2019	2020	2019
	\$	\$	\$	\$
Short-term employee benefits				
Cash salary, fees and short-term compensated absences	8,089,907	6,487,358	8,089,907	6,487,358
Short-term cash profit-sharing and other bonuses	1,995,824	4,623,934	1,995,824	4,623,934
Non-monetary benefits	196,786	457,256	196,786	457,256
Other short-term employee benefits	328,519	284,266	328,519	284,266
	10,611,036	11,852,814	10,611,036	11,852,814
Post-employment benefits				
Pension and superannuation benefits	263,656	288,175	263,656	288,175
Other post-employment benefits	84,864	65,061	84,864	65,061
	348,520	353,236	348,520	353,236
	11,308,076	12,206,050	11,308,076	12,206,050
Share based payments granted during the year	4,800,953	1,935,110	4,800,953	1,935,110

#### Other transactions with key management personnel

In addition to their salaries, the consolidated entity also provides non-cash benefits to its key management personnel, and contributes to a post-employment defined contribution plan on their behalf.

Executive officers are eligible to participate in the ultimate chief entity's employee share ownership programmes note 20.

Apart from the details disclosed in this note, no Director has entered into a material contract with the Company or the consolidated entity since the end of the previous financial year and there were no material contracts involving Directors' interests existing at year-end.

#### Loans to key management personnel and their related parties

	Consolidated		Company	
	2020	2019	2020	2019
	\$	\$	\$	\$
The aggregate amount of loans to key management personnel of any entity in the consolidated entity	14,339,624	8,610,959	14,339,624	8,610,959
Loan repayments received	3,793,522	710,432	3,793,522	710,432

## 35 Interest rate benchmark reform: Amendments to AASB 9 and IAS 39 'Financial Instruments'

Interbank offered rates ('IBORs') are used to set interest rates on hundreds of trillions of US dollars of different types of financial transactions and are used extensively for valuation purposes, risk measurement and performance benchmarking.

The UK's Financial Conduct Authority ('FCA') announced, in July 2017, that it will no longer persuade or require banks to submit rates for the London interbank offered rate ('LIBOR') after 2021, and national working groups have been actively discussing the mechanisms for an orderly transition of the five relevant LIBOR to their chosen replacement rates. Other regulators globally continue to assess their benchmarks with proposals to demise or re-form them with specific timelines emerging.

Substantial efforts have been undertaken to develop products that reference the replacement rates and enable the transition of legacy lbor contracts which exposes HSBC to material execution, financial and non-financial risks. Throughout 2020, the lbor transition programme has continued to implement the required IT and operational changes necessary for an orderly transition from demising IBORs to the replacement near risk free rates ('RFRs'). The programme now covers transition from 12 interest rate benchmarks including five London interbank offered rate ('LIBOR') currencies, four ASP benchmarks that reference US dollar LIBOR and the Euro Overnight Index Average ('Eonia').

The global lbor transition programme is in place to facilitate an orderly transition to replacement rates for our business and our clients. Development of, and transition to alternative rate products is supported by extensive training, communication and client engagement to facilitate appropriate selection of products. IT and operational change is being implemented to enable a longer transition window. Business line risks have been assessed and are dynamically monitored and overseen, with specific mitigation linked to programme deliverables.

As the majority of the assets and liabilities are in Australian dollars, and BBSW is not a rate that is changing, the impact of the change is not expected to be material.

## 36 Customer relief programmes

In response to the COVID-19 outbreak, governments and regulators around the world have introduced a number of support measures for both personal and wholesale customers in market-wide schemes. The Bank offered such schemes to both personal and wholesale customers in Australia.

The initial granting of customer relief does not automatically trigger a migration to stage 2 or 3. However, information provided by payment deferrals is considered in the context of other reasonable and supportable information. This forms part of the overall assessment for whether there has been a significant increase in credit risk and credit impairment to identify loans for which lifetime ECL is appropriate. An extension in payment deferral does not automatically result in a migration to stage 2 or stage 3. The key accounting and credit risk judgement to ascertain whether a significant increase in credit risk has occurred is whether the economic effects of the COVID-19 outbreak on the customer are likely to be temporary over the lifetime of the loan, and whether they indicate that a concession is being made in respect of financial difficulty that would be consistent with Stage 3.

The following table presents the number of personal accounts/wholesale customers and the associated drawn loan values of customers under these schemes at 31 December 2020.

### Personal lending <sup>(1)</sup>

Extant at 31 December 2020		Total
HSBC-specific measures		
Number of accounts in mortgage customer relief		647
Drawn loan value of accounts in mortgage customer relief	\$m	337.0
Number of accounts in other personal lending customer relief		1,498
Drawn loan value of accounts in other personal lending customer relief	\$m	12.9

### Wholesale lending

Extant at 31 December 2020		Total
HSBC-specific schemes		
Number of customers under HSBC-specific measures		1
Drawn loan value of customers under HSBC-specific measures	\$m	0.3

<sup>1</sup> Schemes for Mortgages, Credit Cards and personal loans such as Payment Pause, Indulgence program and Reduced payments with interest relief were primarily aimed at providing deferment of principal, and interest and/or both. Initially these were 3-6 months and were extended for some customers for an additional 4 months.

## 37 Subsequent events

There has not arisen in the interval between the end of the financial year and the date of this report, any item, transaction or event of a material and unusual nature likely, in the opinion of the Directors of the Company, to affect significantly the operations of the consolidated entity, the results of those operations, or the state of affairs of the consolidated entity, in future financial years.

## Directors' declaration

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### Directors' declaration

In the opinion of the Directors of HSBC Bank Australia Limited:

- the financial statements and notes set out on pages 4 to 57 are in accordance with the Corporations Act 2001, including:
  - giving a true and fair view of the financial position of the Company and the consolidated entity as at 31 December 2020, and of their performance, as represented by the results of their operations and their cash flows, for the year ended on that date; and
  - complying with Australian Accounting Standards and the Corporations Regulations 2001; and
- there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable; and
- the financial report also complies with International Financial Reporting Standards as disclosed in note 2(a).

Dated at Sydney this 15 February 2021.

Signed in accordance with a resolution of the Directors:



**Grant King**  
Chairman



**Kaber Mclean**  
Director

## Independent auditor's report

To the members of HSBC Bank Australia Limited

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### Our opinion

In our opinion:

The accompanying financial report of HSBC Bank Australia Limited (the Company) and its controlled entities (together the Consolidated entity) is in accordance with the *Corporations Act 2001*, including:

- (a) giving a true and fair view of the Company's and Consolidated entity's financial positions as at 31 December 2020 and of their financial performance for the year then ended
- (b) complying with Australian Accounting Standards and the *Corporations Regulations 2001*.

### What we have audited

The financial report comprises:

- the Consolidated and Company statements of financial position as at 31 December 2020
- the Consolidated and Company income statements for the year then ended
- the Consolidated and Company statements of comprehensive income for the year then ended
- the Consolidated and Company statements of changes in equity for the year then ended
- the Consolidated and Company statements of cash flows for the year then ended
- the notes to the financial statements, which include significant accounting policies and other explanatory information
- the directors' declaration.

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### Basis for opinion

We conducted our audit in accordance with Australian Auditing Standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial report* section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### Independence

We are independent of the Company and the Consolidated entity in accordance with the auditor independence requirements of the *Corporations Act 2001* and the ethical requirements of the Accounting Professional & Ethical Standards Board's APES 110 *Code of Ethics for Professional Accountants (including Independence Standards)* (the Code) that are relevant to our audit of the financial report in Australia. We have also fulfilled our other ethical responsibilities in accordance with the Code.

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### Other information

The directors are responsible for the other information. The other information comprises the information included in the annual report for the year ended 31 December 2020, but does not include the financial report and our auditor's report thereon.

Our opinion on the financial report does not cover the other information and accordingly we do not express any form of assurance conclusion thereon.

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**PricewaterhouseCoopers, ABN 52 780 433 757**

One International Towers Sydney, Watermans Quay, Barangaroo, GPO BOX 2650, SYDNEY NSW 2001

T: +61 2 8266 0000, F: +61 2 8266 9999, [www.pwc.com.au](http://www.pwc.com.au)

Level 11, 1PSQ, 169 Macquarie Street, Parramatta NSW 2150, PO Box 1155 Parramatta NSW 2124

T: +61 2 9659 2476, F: +61 2 8266 9999, [www.pwc.com.au](http://www.pwc.com.au)

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In connection with our audit of the financial report, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial report or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work we have performed on the other information that we obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

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### *Responsibilities of the directors for the financial report*

The directors of the Company are responsible for the preparation of the financial report that gives a true and fair view in accordance with Australian Accounting Standards and the *Corporations Act 2001* and for such internal control as the directors determine is necessary to enable the preparation of the financial report that gives a true and fair view and is free from material misstatement, whether due to fraud or error.

In preparing the financial report, the directors are responsible for assessing the ability of the Company and the Consolidated entity to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Company or the Consolidated entity or to cease operations, or have no realistic alternative but to do so.

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### *Auditor's responsibilities for the audit of the financial report*

Our objectives are to obtain reasonable assurance about whether the financial report as a whole is free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with the Australian Auditing Standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial report.

A further description of our responsibilities for the audit of the financial report is located at the Auditing and Assurance Standards Board website at: [http://www.auasb.gov.au/auditors\\_responsibilities/ar3.pdf](http://www.auasb.gov.au/auditors_responsibilities/ar3.pdf). This description forms part of our auditor's report.

### *Matters relating to the electronic presentation of the audited financial report*

This auditor's report relates to the financial report of HSBC Bank Australia Limited for the year ended 31 December 2020 included on HSBC Bank Australia Limited's web site. The directors of the Company are responsible for the integrity of HSBC Bank Australia Limited's web site. We have not been engaged to report on the integrity of this web site. The auditor's report refers only to the financial report named above. It does not provide an opinion on any other information which may have been hyperlinked to/from the financial report. If users of this report are concerned with the inherent risks arising from electronic data communications they are advised to refer to the hard copy of the audited financial report to confirm the information included in the audited financial report presented on this web site.



PricewaterhouseCoopers



Elizabeth O'Brien  
Partner

Sydney  
15 February 2021



## *Auditor's Independence Declaration*

As lead auditor for the audit of HSBC Bank Australia Limited for the year ended 31 December 2020, I declare that to the best of my knowledge and belief, there have been:

- (a) no contraventions of the auditor independence requirements of the *Corporations Act 2001* in relation to the audit; and
- (b) no contraventions of any applicable code of professional conduct in relation to the audit.

This declaration is in respect of HSBC Bank Australia Limited and the entities it controlled during the year.

Elizabeth O'Brien  
Partner  
PricewaterhouseCoopers

Sydney  
15 February 2021

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**PricewaterhouseCoopers, ABN 52 780 433 757**

One International Towers Sydney, Watermans Quay, Barangaroo, GPO BOX 2650, SYDNEY NSW 2001

T: +61 2 8266 0000, F: +61 2 8266 9999, [www.pwc.com.au](http://www.pwc.com.au)

Level 11, 1PSQ, 169 Macquarie Street, Parramatta NSW 2150, PO Box 1155 Parramatta NSW 2124

T: +61 2 9659 2476, F: +61 2 8266 9999, [www.pwc.com.au](http://www.pwc.com.au)

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**HSBC Bank Australia Ltd**

**A.B.N. 48 006 434 162**

International Towers Sydney T1  
100 Barangaroo Avenue  
Sydney  
New South Wales 2000  
Australia  
[www.hsbc.com.au](http://www.hsbc.com.au)