HSBC

News Release

28 July 2021

GRUPO FINANCIERO HSBC, S.A. DE C.V.
FIRST HALF 2021 FINANCIAL RESULTS HIGHLIGHTS

- For the first half of 2021, Grupo Financiero's profit before tax was MXN7,008m, an increase of MXN2,160m, or 44.6%, compared with MXN4,848m for the same period of 2020.

- For the first half of 2021, net income was MXN5,935m, an increase of MXN2,330m or 64.6%, compared with MXN3,605m for the same period of 2020.

- Total operating income excluding loan impairment charge was MXN23,204m, a decrease of MXN1,144 or 4.7%, compared with MXN24,348m for the same period of 2020.

- Loan impairment charges for the first half of 2021 were MXN1,555m, a decrease of MXN4,232m or 73.1%, compared with MXN5,787m for the same period of 2020. During the period there was a release of MXN1,908m of additional reserves booked in the second half of 2020 to cover potential losses due to the Covid-19 outbreak, leaving an outstanding balance of MXN775m as of June 2021.

- Administrative and personnel expenses for the first half of 2021 were MXN14,702m, an increase of MXN955m or 6.9%, compared with MXN13,747m for the same period of 2020.

- The cost efficiency ratio was 63.4% for the first half of 2021, compared with 56.5% for the same period of 2020.

- Net loans and advances to customers were MXN359.5bn at 30 June 2021, showing a decrease of MXN47.4bn or 11.7%, compared with MXN406.9bn at 30 June 2020. Total impaired loans as a percentage of gross loans and advances at 30 June 2021 were 2.6%, compared to 2.2% reported at 30 June 2020.

- At 30 June 2021, total deposits were MXN470.9bn, a decrease of MXN68.4bn, or 12.7%, compared with MXN539.3bn as at 30 June 2020.

- Return on equity was 15.6% for the first half of 2021, whereas for the first half to 2020 it was 9.7%.

- At 30 June 2021, the bank's total capital adequacy ratio was 14.3% and the common equity tier 1 capital ratio was 11.9% compared with 13.8% and 11.2%, respectively, at 30 June 2020.

On a reported IFRS basis, for the first half of 2021, profit before tax for the period was MXN7,276m, an increase of MXN9,253m compared with the loss of MXN1,977m reported for the same period in 2020. The increase is mainly driven by lower impairment charges compared to June 2020, when higher impairment charges were recognised as a consequence of IFRS9 Forward Economic Guidance (FEG) due to Covid-19 outbreak.

The main differences between Mexican GAAP and IFRS results for the first half of 2021 relate to differences in loan impairment charges, accounting for fair value adjustments on financial instruments, effective interest rate, deferred profit sharing, additional tier 1 (AT1) instrument valuation and pensions and insurance liabilities.

This news release is issued by
Grupo Financiero HSBC S.A de C.V.

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Covid-19

The Covid-19 outbreak and its effect on the economy have continued to impact our customers and our performance, and the future effects of the pandemic remain uncertain. Renewed outbreaks, as a result of the emergence of the new variants of the virus, emphasise the ongoing threat of Covid-19. We continue to monitor the situation.

Business continuity arrangements have ensured we remain operationally resilient as well as protecting the safety and wellbeing of our staff during the pandemic. The vaccine rollout in Mexico gained traction during the second quarter of 2021 and new Covid-19 cases declined since peaking in December 2020-January 2021, leading to a broad reopening of the economy. Nevertheless, overall vaccination levels are not at the levels needed to achieve herd immunity and ongoing threats from new variants remain.

Payment holidays and other relief programmes adopted to support customers during 2020 have already expired. In wholesale, US$1.2bn (10% of the portfolio) were granted relief of which 8% of the Corporate portfolio and 30% of the Business Banking portfolios have subsequently been classified as non-performing loans (NPLs). For Wealth and Personal Banking (WPB) portfolios, relief programmes totalled US$1.3bn (circa 20% of the portfolio) of which 80% have returned to regular payment and 20% are still show varying levels of distress (either received an extension or missed at least one instalment).

At 30 June 2021, our capital and liquidity ratios remain solid, allowing us to continue supporting our customers throughout the Covid-19 outbreak.

HSBC Pensiones Business

Grupo Financiero HSBC, through HSBC Pensiones SA, whose direct controller is HSBC Seguros, SA has received regulatory approval from COFECE (Comisión Federal de Competencia Económica) and CNSF (Comisión Nacional de Seguros y Fianzas) to transfer its pension insurance policies. The transfer will be made to Pensiones Banorte SA Grupo Financiero Banorte following the agreement signed in 2020.

Overview

The Mexican economy remained on a recovery path in 2Q21, mainly driven by a better-than-expected performance of service sector activities. Meanwhile, industrial production has moderated, as most of the positive impact from the recovery in the US was incorporated during 2H20 and 1Q21. In fact, domestic-related industrial activities have improved in recent months. Overall, the gradual lifting of restrictions related to the pandemic proved supportive for domestic activities in 2Q21.

Inflation climbed to 5.88% year over year by the end of 2Q21 from 4.67% in 1Q21. Higher prices in both core and non-core components were the main drivers. In particular, an acceleration in core inflation, driven by higher tradable goods and services prices, prompted higher-than-expected inflation prints in 2Q21. The annual inflation rate remains well above Mexico's central bank's (Banxico) mid-point inflation target of 3.0%.

In light of this, Banxico lifted the monetary policy rate by 25bp to 4.25% on 24 June, in a divided board decision of 3-2. This move responded to the gradual deterioration of short-term inflation expectations.

Financial Performance – Key Metrics

- For the first half of 2021, Grupo Financiero's profit before tax was MXN7,008m, an increase of MXN2,160m, or 44.6%, compared with MXN4,848m for the same period of 2020.

- Net interest income for the first half of 2021 was MXN16,641m, a decrease of MXN663m or 3.8%, compared with the same period of 2020. The decrease is mainly due to lower loan portfolio volumes as well as lower interest rates partially offset by a decrease in funding costs driven by the reduction in Central Bank reference interest rate and decrease in wholesale funding. In addition, net interest income reduced due to Insurance business reporting higher insurance claims and technical reserves impacted by Covid-19 partially offset by higher premiums.

- Loan impairment charges for the first half of 2021 were MXN1,555m, a decrease of MXN4,232m or 73.1%, compared with MXN5,787m for the same period of 2020. During the period there was a release of MXN1,908m of additional reserves booked in the second half of 2020 to cover potential losses due to Covid-19 outbreak, of which MXN1,088m in retail and MXN820m in wholesale, coupled by better performance in early delinquency across all portfolios and lower wholesale portfolios.

- Net fee income for the first half of 2021 was MXN4,012m, an increase of MXN126m, or 3.2%, compared with same period of 2020, mainly driven by higher loan portfolio and asset management fees.

- Trading income for the first half of 2021 was MXN1,943m, a decrease of MXN763m, or 28.2%, compared with the same period of 2020, mainly driven by lower derivatives results.

- Other operating income for the first half of 2021 was MXN608m, an increase of MXN156m, or 34.5%, compared with the same period of 2020, driven primarily by the sale of a real estate company.

- Administrative and personnel expenses for the first half of 2021 were MXN14,702m, an increase of MXN955m, or 6.9%, compared with MXN13,747m for the same period of 2020, mainly driven by higher staff and IT costs.

- The cost efficiency ratio was 63.4% for the first half of 2021, compared with 56.5% for the same period of 2020.

- The effective tax rate was 15.3% for the first half of 2021, compared with 25.6% reported for the same period of 2020, the decrease is driven mainly by the effect of inflationary adjustments and deferred tax asset movements.

- Net loans and advances to customers were MXN359.5bn at 30 June 2021, showing a decrease of MXN47.4bn, or 11.7% compared with MXN406.9bn at 30 June 2020. The performing corporate portfolio observed a reduction of 23.3%, with respect to 30 June 2021 mainly driven by the decrease in commercial loans. The performing retail portfolio increased by 15.2% with respect to 30 June 2020 driven by mortgage loans growing 26.5%, coupled with a slight increase in consumer loans by 2.6%. Credit cost ratios[1/] and loan loss reserves ratios[2/] as of June 2021 were 0.8% (2.7% as of June 2020) and 4.2% (3.4% as of June 2020), respectively.

- Total impaired loans as a percentage of gross loans and advances at 30 June 2021 was 2.6%, compared to 2.2% at 30 June 2020.

- Return on equity was 15.6% for the first half of 2021, whereas for the first half of 2020 it was 9.7%, mainly driven by a higher profit-after-tax.

- Total loan loss allowances at 30 June 2021 were MXN15.9bn, an increase of MXN1.6bn or 11.2% compared to 30 June 2020. The total coverage ratio (allowance for loan losses divided by impaired loans) was 161.9% at 30 June 2021, compared with 154.5% at 30 June 2020.

- As of 30 June 2021, total deposits were MXN470.9bn, a decrease of MXN68.4bn or 12.7%, compared with MXN539.3bn at 30 June 2020 mainly driven by reduction in wholesale funding, improving the blended cost of funds.

- HSBC Bank Mexico profit before tax for the first half of 2021 was MXN5,371m, an increase of MXN1,144m or 27.1% compared with the same period of 2020 mainly driven by lower loan impairment charges partially offset by lower trading income and higher expenses.

- HSBC Bank Mexico net profit for the first half of 2021 was MXN4,734m, an increase of MXN1,570m or 49.6% compared with the same period of 2020.

- HSBC Bank Mexico net interest income for the first half of 2021 was MXN15,965m a decrease of MXN619m or 3.7%, compared with the same period of 2020.

- At 30 June 2021, the bank's total capital adequacy ratio was 14.3% and the common equity tier 1 capital ratio was 11.9%, compared with 13.8% and 11.2%, respectively, at 30 June 2020. HSBC's global strategy is to work with optimal levels of capital with a reasonable buffer above regulatory limits.

- The profit before tax of Grupo Financiero HSBC's insurance subsidiary for the first half of 2021 was MXN1,014m, an increase of MXN669m when compared to same period of 2020, mainly driven by higher trading income and higher premiums partially offset by higher claims and technical reserves impacted by Covid-19.

[1/] Credit Cost Ratio: Loan Impairment charges (annualised)/Gross Loans.

[2/] Loan Loss Reserve Ratio: Loan Loss Reserves/Gross Loans.

HSBC Mexico S.A. (the bank) is a subsidiary of Grupo Financiero HSBC, S.A. de C.V. (Grupo Financiero HSBC) and is subject to supervision by the Mexican Banking and Securities Commission. The bank is required to file financial information on a quarterly basis (in this case for the period ended 30 June 2021) and this information is publicly available. Given that this information is available in the public domain, Grupo Financiero HSBC has elected to file this release. HSBC Seguros, S.A. de C.V. Grupo Financiero HSBC (HSBC Seguros) is Grupo Financiero HSBC's insurance subsidiary.

All numbers are as reported and there were no significant items distorting period-on-period comparisons, with the exception of the impact of the gain on sale of the acquiring business recognised in Other Income.

Results are prepared in accordance with Mexican GAAP (Generally Accepted Accounting Principles).

Business highlights [1/] *(Amounts described include the impact of internal cost and value of funds applied to different lines of business. For comments on general expenses variances, please refer to the financial overview for Grupo Financiero).*

Wealth and Personal Banking (WPB) [2/]

WPB revenues decreased by 3.4% compared to the same period of last year, mainly driven by higher insurance claims due to Covid-19 pandemic environment and lower sales, central bank rate cuts affecting liabilities coupled with lower volumes in business banking and term deposits. This was partially offset by higher demand deposits and mortgages volumes, higher mutual fund balances and trading income in the Pensions business.

Loan impairment charges during the period were MXN2,822m, a decrease of MXN1,833m or 40%, compared with MXN4,705m for the same period of 2020. The first half included a release of MXN1,088m of additional reserves booked in the second half of 2020 to cover potential losses due to Covid-19 outbreak, leaving an outstanding balance of MXN207m as of June 2021.

WPB profit before tax for the first half of 2021 was MXN1,386m, an increase of MXN431m compared to the same period of 2020 (with markets treasury reallocation, profit before tax result was MXN1,899m). The increase is mainly driven by lower loan impairments charges due to provisions release.

Mortgage portfolio grew 26.5% compared to first half of 2020, with sales being 92.0% higher than previous year. We maintain a high level of productivity through the different commercial channels, such as the branch network, mortgage brokers and developers. HSBC continues to participate with the government in the sales of loans through FOVISSSTE (Mexican government housing agency)

Demand deposits grew by 18.0% and mutual funds by 4.0% compared to the same period of 2020. The recommendation index (based on the 'net promoter score' methodology) continues to trend upward in Branches, Premier-Advance, Digital Channels and ATMs.

HSBC continues to cooperate and align with the government guidelines in order to ensure the banking services as an essential activity. Currently, most of our branches are opened and operating within the local regulations requirements.

Digital Banking, Contact Center and ATMs continue to offer services in accordance to demand. Cash deposit machines (CDMs) option is open for clients to carry out their transactions without visiting the branch, and is accessible on all days of a week. In branches, tablets and biometrics usage keep providing great support, to improve remote operation capability. It is worth to highlight that CoDi, a digital payments functionality promoted by Mexican Central Bank since October 2019, has been launched in HSBC through Mobile Banking from 4Q20

Commercial Banking (CMB)

Revenues for the first half of the year reduced by 2.1% compared to the same period of 2020. This is the result of a low interest rate environment reducing our Deposit margins and also resulting on a reduction from Customer Loans and Deposit Balances. These impacts were partly offset by an increase on commercial activity providing higher fee & trading income, coupled with higher spreads and lower cost of funds.

Loan impairment charges during the period were MXN462m, a decrease of MXN1,022m or more than 100%, compared with MXN560m for the same period of 2020. The first half included a release of MXN714m of additional reserves booked in the second half of 2020 to cover potential losses due to Covid-19 outbreak, leaving an outstanding balance of MXN494m as of June 2021.

Profit before tax was MXN1,931m, an increase of MXN1,063m or over 100% compared with the same period of 2020. The increase is primarily driven by the release in credit provisions combined with lower expense base. With Markets Treasury allocation, profit before tax for the current period was MXN2,173m.

Global Banking and Markets (GB&M)

Revenues for the first half of the year up to 30 June 2021 reduced by 31.3% compared with the same period of 2020, mostly explained by derivatives business, lower revenues from deposits due to the low interest rate environment and lower portfolio balances.

In 2021, loan impairment charges reduced by more than 100% explained by releases of MXN805m in provisions, mainly driven by portfolio reductions.

GB&M maintained its strategic focus on the cross-sale of products including Global Markets solutions, Trade Services and Liquidity and Cash Management, with an operating model that leverages from our international footprint and global capabilities thus allowing us to capture relevant transactions with international customers.

Profit before tax was MXN1,787m, an increase of MXN212m or 13.5% compared with the same period of 2020, mainly driven by decrease on credit provisions. With Markets Treasury allocation, profit before tax for the current period was MXN1,998m.

1/ *In 2020, BSM (Balance Sheet Management) was renamed to Markets Treasury. Markets Treasury total profit before tax for the six months ended at 30 of June 2021 was MXN966m. Since June 2020, Markets Treasury is allocated out to the global businesses, to align them better with their revenue and expense and for the six months to 30 of June 2021 profit before tax allocation by business was – MXN513m to WPB, MXN242m to CMB and MXN211m to GB&M.*

2/ *As part of the Strategic announcements made by HSBC Group Executive Committee, 'RBWM – Retail Banking and Wealth Management and GPB – Global Private Banking' line of business is merged to create one new line of business, 'WPB – Wealth and Personal Banking'.*

Grupo Financiero HSBC's six months to 2021 financial results as reported to HSBC Holdings plc, our ultimate parent company, are prepared in accordance with International Financial Reporting Standards (IFRS).

On a reported IFRS basis, for the six months to 30 June 2021, profit before tax for the period was MXN7,276m, an increase of MXN9,253m compared to the same period in 2020. The increase is mainly driven by lower impairment charges compared to June 2020, when higher impairment charges were created as a consequence of IFRS9 Forward Economic Guidance (FEG) due to Covid-19 outbreak.

The main differences between Mexican GAAP and IFRS results for the six months to June 2021 relate to differences in loan impairment charges, accounting for fair value adjustments on financial instruments, effective interest rate, deferred profit sharing, AT1 instrument valuation and pensions and insurance liabilities.

About HSBC

Grupo Financiero HSBC is one of the leading financial groups in Mexico with 921 branches, 5,539 ATMs and 15,135 employees[1]. For more information, visit www.hsbc.com.mx.

HSBC Holdings plc, the parent company of HSBC, is headquartered in London. HSBC serves customers worldwide from offices in 64 countries and territories in our geographical regions: Europe, Asia, North America, Latin America, and Middle East and North Africa. With assets of US$2,959bn at 31 March 2021, HSBC is one of the world's largest banking and financial services organisation.

[1/] As of June 2021, the total employees count of 15,135 includes 1,041 employees who are hired by Electronic Data Process Mexico S.A. de CV, a subsidiary of HSBC Global Services Limited.

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Consolidated Income Statement – GROUP six months ended 30 June 2021 and 2020

Figures in MXN millions

	Group	
	30 Jun 2021	**30 Jun 2020**
Interest income	26,239	30,721
Interest expense	(9,598)	(13,417)
Net interest income	16,641	17,304
Loan impairment charges	(1,555)	(5,787)
Risk-adjusted net interest income	15,086	11,517
Fees and commissions receivable	5,376	5,135
Fees payable	(1,364)	(1,249)
Trading income	1,943	2,706
Other operating income	608	452
Total operating income	21,649	18,561
Administrative and personnel expenses	(14,702)	(13,747)
Net operating income	6,947	4,814
Share of profits in equity interest	61	34
Profit/loss before tax	7,008	4,848
Income tax	(829)	(1,241)
Deferred income tax	(244)	(2)
Net income	5,935	3,605

Consolidated Income Statement – BANK six months ended 30 June 2021 and 2020

Figures in MXN millions

	Bank	
	30 Jun 2021	**30 Jun 2020**
Interest income	22,861	28,874
Interest expense	(6,896)	(12,290)
Net interest income	15,965	16,584
Loan impairment charges	(1,555)	(5,787)
Risk-adjusted net interest income	14,410	10,797
Fees and commissions receivable	5,074	4,886
Fees payable	(1,469)	(1,335)
Trading income	1,129	2,676
Other operating income	720	831
Total operating income	19,864	17,855
Administrative and personnel expenses	(14,557)	(13,662)
Net operating income	5,307	4,193
Share of profits in equity interest	64	34
Profit/loss before tax	5,371	4,227
Income tax	(402)	(1,056)
Deferred income tax	(235)	(7)
Net income	4,734	3,164

Consolidated Balance Sheet

Figures in MXN millions	Group		Bank	
	30 Jun 2021	**30 Jun 2020**	**30 Jun 2021**	**30 Jun 2020**
Assets				
Cash and deposits in banks	54,967	45,551	54,845	46,383
Margin accounts	224	292	224	292
Investment in securities	**180,455**	**184,832**	**162,618**	**168,481**
Trading securities	74,363	53,878	71,530	52,125
Available-for-sale securities	78,337	102,863	72,054	97,512
Held to maturity securities	27,755	28,091	19,034	18,844
Repurchase agreements	48,910	59,369	48,910	59,369
Derivative transactions	46,469	107,266	46,469	107,266
Performing loans				
Commercial loans	175,369	233,323	175,369	233,323
Loans to financial intermediaries	8,916	16,481	8,916	16,481
Loans to government entities	32,714	33,180	32,714	33,180
Consumer loans	62,684	61,087	62,684	61,087
Mortgage loans	85,923	67,912	85,923	67,912
Total performing loans	**365,606**	**411,983**	**365,606**	**411,983**
Impaired loans				
Commercial loans	4,978	4,574	4,978	4,574
Consumer loans	1,871	2,675	1,871	2,675
Mortgage loans	2,993	2,033	2,993	2,033
Total impaired loans	**9,842**	**9,282**	**9,842**	**9,282**
Gross loans and advances to customers	**375,448**	**421,265**	**375,448**	**421,265**
Allowance for loan losses	(15,938)	(14,339)	(15,938)	(14,339)
Net loans and advances to customers	**359,510**	**406,926**	**359,510**	**406,926**
Accounts receivables from Insurers and Bonding companies	89	71	-	-
Premium receivables	1,767	1,629	-	-
Accounts receivables from reinsurers and rebonding companies	38	19	-	-
Other accounts receivable	42,741	34,672	42,613	35,744
Foreclosed assets	333	337	333	337
Property, furniture and equipment, net	4,857	4,349	4,857	4,349
Long-term investments in equity securities	1,035	993	995	957
Long-term assets available for sale	-	471	-	240
Deferred taxes	10,645	11,116	10,503	10,968
Goodwill	1,048	1,048	-	-
Other assets, deferred charges and intangibles	7,108	5,552	6,754	5,416
Total assets	**760,196**	**864,493**	**738,631**	**846,728**

Consolidated Balance Sheet (continued)

Figures in MXN millions	Group 30 Jun 2021	Group 30 Jun 2020	Bank 30 Jun 2021	Bank 30 Jun 2020
Liabilities				
Deposits	**470,918**	**539,307**	**473,805**	**540,875**
Demand deposits	309,397	312,853	311,934	313,932
Time deposits	137,743	176,029	137,352	175,643
Bank bond outstanding	23,778	50,425	23,778	50,425
Global deposit account without movements			741	875
Bank deposits and other liabilities	**27,937**	**38,982**	**27,937**	**38,983**
On demand	12,271	2,488	12,271	2,488
Short-term	10,964	7,044	10,964	7,045
Long-term	4,702	29,450	4,702	29,450
Repurchase agreements	21,281	29,069	21,281	29,069
Collateral sold	17,453	3,684	17,453	3,684
Derivative transactions	40,812	105,013	40,812	105,013
Technical reserves	15,201	13,111	-	-
Accounts payable from reinsures and rebounding companies	3	5	-	-
Other payable accounts	**76,028**	**44,588**	**75,196**	**45,257**
Income tax and employee profit sharing payable	617	592	477	563
Sundry creditors and other accounts Payable	75,411	43,996	74,719	44,694
Subordinated debentures outstanding	11,566	13,418	11,566	13,418
Deferred credits and receivable in advance	1,270	1,512	1,163	1,403
Total liabilities	**682,469**	**788,689**	**669,213**	**777,702**
Equity				
Paid in capital	**43,373**	**43,373**	**38,318**	**38,318**
Capital stock	6,218	6,218	6,132	6,132
Additional paid in capital	37,155	37,155	32,186	32,186
Other reserves	**34,349**	**32,439**	**31,098**	**30,705**
Capital reserves	1,244	1,244	13,202	13,191
Retained earnings	28,546	28,822	16,531	17,524
Result from the mark-to-market of available-for-sale securities	(789)	(872)	(828)	(1,031)
Result from cash flow hedging transactions	(587)	(360)	(587)	(360)
Adjustment in the employee pension	-	-	(1,954)	(1,784)
Net income	5,935	3,605	4,734	3,164
Minority interest in capital	5	(8)	2	4
Total equity	**77,727**	**75,804**	**69,418**	**69,026**
Total liabilities and equity	**760,196**	**864,493**	**738,631**	**846,728**

Consolidated Balance Sheet (continued)

	Group		Bank	
Figures in MXN millions	**30 Jun 2021**	**30 Jun 2020**	**30 Jun 2021**	**30 Jun 2020**
Memorandum Accounts	**5,098,744**	**6,549,012**	**4,903,581**	**6,367,351**
Third party accounts	**29,712**	**27,914**	**27,213**	**26,068**
Clients current accounts	1,564	1,022	-	-
Custody operations	935	824	-	-
Third party investment banking operations, net	27,213	26,068	27,213	26,068
Proprietary position	**5,069,032**	**6,521,098**	**4,876,368**	**6,341,283**
Irrevocable lines of credit granted	273,730	328,366	273,730	328,366
Goods in trust or mandate	181,063	204,182	181,063	204,182
Goods in custody or under administration	1,452,476	1,358,551	1,446,258	1,352,334
Collateral received by the institution	88,875	76,800	88,875	76,800
Collateral received and sold or delivered as guarantee	45,065	15,215	45,065	15,215
Suspended interest on impaired loans	389	276	389	276
Other control accounts	3,027,434	4,537,708	2,840,988	4,364,110

Consolidated Statement of Changes in Shareholders' Equity

GROUP *Figures in MXN million*	Capital contributed	Capital Reserves	Retained earnings	Result from valuation of available-for-sale securities	Result from cash flow hedging transactions	Net Income	Minority interest	**Total Equity**
Total Balances at 31 Dec 2020	**43,373**	**1,244**	**28,157**	**(283)**	**(93)**	**63**	**7**	**72,468**
Movements inherent to the shareholders' decision								
Transfer of result of prior years	-	-	63	-	-	(63)	-	**-**
Others	-	-	22	-	-	-	-	**22**
Total	**-**	**-**	**85**	**-**	**-**	**(63)**	**-**	**22**
Movements for the recognition of the comprehensive income								
Net income	-	-	-	-	-	5,935	-	**5,935**
Result from valuation of available-for-sale securities	-	-	-	(506)	-	-	-	**(506)**
Result from cash flow hedging transactions	-	-	-	-	(494)	-	-	**(494)**
Others*	-	-	304		-		(2)	**302**
Total	**-**	**-**	**304**	**(506)**	**(494)**	**5,935**	**(2)**	**5,237**
Total Balances at 30 Jun 2021	**43,373**	**1,244**	**28,546**	**(789)**	**(587)**	**5,935**	**5**	**77,727**

**Includes local pension plan and valuation on technical risk reserves from Insurance entity*

Consolidated Statement of Changes in Shareholders' Equity

BANK	Capital contributed	Capital reserves	Retained earnings	Result from valuation of available-for-sale securities	Result from cash flow hedging transactions	Adjustment in defined benefit pension plan	Net income	Minority interest	Total equity
Figures in MXN million									
Total Balances at 31 Dec 2020	**38,318**	**13,202**	**17,373**	**(477)**	**(93)**	**(2,249)**	**(709)**	**5**	**65,370**
Movements inherent to the shareholders' decision									
Transfer of result of prior years	-		(709)	-	-	-	709	-	**-**
Others	-	-	-	-	-	-	-	-	-
Total	**-**	**-**	**(709)**	**-**	**-**	**-**	**709**	**-**	**-**
Movements for the recognition of the comprehensive income									
Net income	-	-	-	-	-	-	4,734	-	**4,734**
Result from valuation of available-for-sale securities	-	-	-	(351)	-	-	-	-	**(351)**
Result from cash flow hedging transactions	-	-	-	-	(494)	-	-	-	**(494)**
Adjustment in defined benefit pension plan	-	-	-	-	-	295	-	-	**295**
Others			(133)					(3)	**(136)**
Total	**-**	**-**	**(133)**	**(351)**	**(494)**	**295**	**4,734**	**(3)**	**4,048**
Total Balances at 30 Jun 2021	**38,318**	**13,202**	**16,531**	**(828)**	**(587)**	**(1,954)**	**4,734**	**2**	**69,418**

Consolidated Statement of Cash Flows Group

Figures in MXN millions	**30 Jun 2021**
Net income	**5,935**
Adjustments for items not involving cash flow:	**3,241**
Allowances for loan losses	1,555
Depreciation and amortisation	1,105
Valuations	(2,766)
Technical reserves	1,218
Provisions	1,117
Income Tax and deferred taxes	1,073
Participation in the Results of Unconsolidated Subsidiaries	(61)
Changes in items related to operating activities:	
Margin accounts	19
Investment securities	9,774
Repurchase agreements	23,390
Derivative (assets)	29,288
Loan portfolio	(12,301)
Foreclosed assets	16
Operating assets	(7,037)
Deposits	(24,884)
Bank deposits and other liabilities	8,782
Creditors repo transactions	(23,851)
Collateral sold or delivered as guarantee	15,829
Derivative (liabilities)	(20,858)
Accounts receivables from reinsurers and coinsurers	(9)
Accounts receivables from premiums	83
Other operating liabilities	(2,308)
Income tax paid	(589)
Funds provided by operating activities	**(4,656)**
Investing activities:	
Acquisition of property, furniture and equipment	(746)
Intangible assets acquisitions & Prepaid expenses	(1,627)
Cash dividends	37
Proceeds on disposal of subsidiaries	605
Other investment activities	(213)
Funds used in investing activities	**(1,944)**
Financing activities:	
Others	(133)
Funds used in financing activities	**(133)**
Financing activities:	
Increase/decrease in cash and equivalents	2,443
Cash and equivalents at beginning of period	52,524
Cash and equivalents at end of period	**54,967**

Consolidated Statement of Cash Flows Bank

Figures in MXN millions	**30 Jun 2021**
Net income	**4,734**
Adjustments for items not involving cash flow:	**(404)**
Allowances for loan losses	1,555
Valuations	(2,575)
Depreciation	525
Amortisation	580
Provisions	(1,062)
Income Tax and deferred taxes	637
Share of profits in equity interest	(64)
Changes in items related to operating activities:	
Margin accounts	19
Investment securities	11,951
Repurchase agreements	23,390
Derivative (assets)	29,288
Loan portfolio	(12,301)
Foreclosed assets	16
Operating assets	(6,910)
Deposits	(23,996)
Bank deposits and other liabilities	8,782
Creditors repo transactions	(23,851)
Collateral sold or delivered as guarantee	15,829
Derivative (liabilities)	(20,858)
Subordinated debentures outstanding	(2)
Other operating liabilities	(387)
Income tax paid	(378)
Funds provided by operating activities	**4,922**
Investing activities:	
Proceeds on disposal of property, furniture and equipment	
Acquisition of property, furniture and equipment	(746)
Intangible assets acquisitions & Prepaid expenses	(1,627)
Cash dividends	37
Other investment activities	(3)
Funds used in investing activities	**(2,339)**
Financing activities:	
Others	(133)
Funds used in financing activities	**(133)**
Financing activities:	
Increase/decrease in cash and equivalents	**2,450**
Cash and equivalents at beginning of period	52,395
Cash and equivalents at end of period	**54,845**

Changes in Mexican accounting standards

Introduction

Grupo Financiero HSBC consolidated financial statements are prepared in accordance with the accounting standards applicable to financial group holding companies in Mexico, they are issued by the National Banking and Securities Commission (CNBV for its acronym in Spanish). Those accounting standards are based on the Financial Reporting Standards (NIF for its acronym in Spanish) issued by the Mexican Financial Reporting Standards Council (CINIF for its acronym in Spanish), but including specific rules for accounting, valuation, presentation and disclosure for particular financial institutions transactions, which in some cases are different.

Subsidiaries financial statements were prepared in accordance with accounting standards issued by CNBV applicable to banks, excepting by the Insurance Company (HSBC Seguros) which are prepared in line with accounting standards issued by National Insurance and Bonding Commission (CNSF for its acronym in Spanish).

The recent changes in accounting standards issued by CNBV or CINIF applicable to Grupo Financiero HSBC, are described below:

I. Improvements of NIF 2021 issued by CINIF applicable to Financial Institutions.

CINIF issued a document called 'Improvements of NIF 2021', which mainly includes the following changes and improvements:

Improvements involving accounting changes 'without financial impacts' in Grupo Financiero HSBC.

NIF C-2 'Financial Instruments' – The option to irrevocable designation of measurement at fair value through Other Comprehensive Income for certain equity instruments not for trading was included in line with IFRS 9.

NIF C-19 'Financial Liabilities' and NIF C-20 'Financial Assets under Hold-to-Collect business model measure at amortised cost' – Gains and losses originated by forgiven amounts in the de-recognition of financial liabilities or renegotiation of financial assets measured at amortised cost should be presented separately in income statement within operating activities line.

Also, a clarification was included to determine that interest, commissions and other concepts paid in advance are not considered as part of transactional costs in the origination of financial assets and liabilities.

NIF D-5 'Leases' – Inclusion of special disclosures for short-term and low-value leases which are part of the exemption to not to apply the lease accounting model. Elimination of disclosures about lease assets that have met 'Investment Properties' definition in the past, given that in the new NIF C-17 'Investment properties' (see below), those leased properties would not meet that definition.

Improvements which not originate accounting changes in Grupo Financiero HSBC

NIF C-8. 'Intangible Assets' and NIF terms chapter– Inclusion of 'amortisable amount' definition which states that it is acquisition cost less residual value and accumulated impairments.

NIF terms chapter – Changes in some definitions such as Amortisation, Depreciation, Inventory, Expected Credit Losses, Free-risk rate and Residual Value.

NIF Interpretations issued by CINIF in 2020

INIF 23. 'Relief for lessees accounting for Covid-19-related rent concessions' – The CINIF issued a relief to account for these rent concessions directly in income statement instead of being considered as a modification of the lease agreement in accordance with NIF D-5 'Leases'. The application of this relief covers rent concessions that reduce only lease payments due on or before 30 June 2021.

INIF 24. 'IBOR Reform' – Given the reform to transit from 'Interbank Offered Rates-IBOR' to Risk-Free-Rates (RFR), the CINIF issued some relief to be applied during the transitional period for financial instruments measured at amortised cost which are referenced to IBOR rates and hedge relationships that hedge IBOR interest rate risk.

The relief indicates that the de-recognition of original financial instrument would not be trigger as long as the new RFR is economic equivalent to the IBOR, i.e. it will generate similar cash flows for the remaining tenor of the instrument and the rest of the changes are part of the reform for financial instruments measured at amortised costs. So, it would only represent an adjustment in the reference rate once the change occurs.

On the other hand, for hedge relationships based on IBOR risks, when the change is to modify the interest rate risk to designate the new RFR, both hedge item and hedge instrument will still exist without discontinuing the hedge relationship.

Financial Institutions have not been adopted the NIF related to INIF 24 yet, instead particular accounting treatment issued by CNBV is applied, nevertheless the IBOR reform would carry financial implications anyway, therefore a position was asked to the regulator, who has confirmed in written, that as long as the changes are exclusively originated by IBOR reform, modified loans would not be subject to recognised as restructured loan as the current accounting standards state.

No significant financial impacts have been observed in the implementation of the changes. It is important to highlight that NIF C-2, C-19, C-20, D-5, INIF 23 and INIF 24 will be in force for Financial Institutions in 2022.

II. New NIF C-17 'Investment Properties'.

The new accounting standard has the purpose to demise the use of IAS 40 'Investment Properties'. The standard indicates that the measurement basis of investment properties: cost or fair value is an accounting policy election, even when in the use of IAS 40 only the cost model was permitted.

There are some differences with guidance provided by IAS 40. One is related to the definition of 'Investment Property' which indicates that to meet this definition, the properties should be held with the main objective of capital appreciation rather than the celebration of lease agreements, while in IAS 40 both could meet the definition.

Additionally, NIF C-17 indicates that an Investment Property would not meet the Right of Use definition under the NIF D-5 'Leases', because typically the lessee will not have the possibility of capital appreciation over the leased property, nevertheless, in IAS 40 the Right of Use over a land or building in a lease agreement under IFRS 16 could be considered an Investment Property.

The new standard was in place 2021. Considering the objective of the properties held by Grupo Financiero HSBC's subsidiaries in Mexico is substantially for rental purposes instead of capital appreciation, the preliminary conclusion reached is that this rule would not have impacts for them in solo accounts. For consolidated accounts, all properties are considered PP&E because are totally used by entities which integrated the group, so no impacts are originated by NIF C-17.

The regulator has not confirmed if the NIF should be adopted as part of changes in CNBV accounting standards in 2022, as described in section below, or from 2021. Regulatory confirmation has not received so far.

III. Changes in CNBV accounting standard A-2 'Aplicación de Normas Particulares.'

Mexican Banking regulator 'CNBV' has completed amendments in accounting standards applicable to Financial Institutions with the objective to converge to IFRS 9 Financial Instruments, IFRS 13 Fair Value and IFRS 15 Revenue from contracts with customers and IFRS 16 Leases. Furthermore, CNBV is planning to adopt the new NIF C-22 Crypto-currencies. As part of the implementation process, CNBV will require the adoption of some NIF already issued by CINIF that include the implementation of these international accounting standards:

NIF B-17 'Fair Value'. This standard includes the different methodologies that entities would use to determine the fair value of the financial instruments maximizing the use of data inputs from observable transactions in the market rather than the use of those non-observable.

NIF C-2 'Investment in Financial Instruments'. Setting out the accounting rules of measurement, presentation and disclosures required for Investment in Financial Instruments. It eliminates the intention as a main driver to determine the classification of the financial instruments and adopts the Business Model framework to manage financial investments.

NIF C-3 'Accounts receivables'. Regarding to the measurement, presentation and disclosures required for accounts receivables.

NIF C-9 'Provisions, Contingent assets and liabilities and commitments". Accounting rules of measurement, presentation and disclosures required for provisions and commitments, excluding the guidance for the accounting of financial liabilities that are included in NIF C-19.

NIF C-10 'Derivative financial instruments and hedge relationship". Including the characteristics to consider a derivative financial instrument for trading or hedging as well as the recognition, measurement, presentation and disclosure.

NIF C-16 'Impairment of financial instruments held to collect principal and interest"**.** Including the accounting standards for measurement, accounting recognition, presentation and disclosures of the impairment of financial instruments hold to collect cash flows. It is important to highlight that the CNBV has worked on special accounting standard which will cover the impairment for loans and advances that are held to collect cash flows, therefore this NIF would be partially adopted by Financial Institutions unless Financial Institution decides to adopt an internal methodology based on NIF C-16 which should be previously approved by CNBV.

NIF C-19 'Financial liabilities''. It includes the accounting standards of the measurement, accounting recognition, presentation and disclosures of financial liabilities. It also includes the methodology of effective interest rate to measure those financial liabilities at amortised cost.

NIF C-20 'Financial instruments hold to collect principal and interest'. Accounting standards about the measurement, accounting recognition, presentation and disclosures of financial instruments hold to collect principal and interest. It eliminates the intention as a main driver to determine the classification of the financial instruments and adopts the Business Model framework to manage financial investments.

NIF C-22 'Crypto-currencies' This new standard provides guidance to initial recognition, measurement and disclosures related to financial transactions with digital-currencies and related costs. In summary, investments in digital-currencies would be recognised initially at acquisition cost with changes in their fair value directly in income statement. Their fair value should be measured in accordance with 'NIF B-17'. Receivable and Payable accounts denominated in digital-currencies would be measured initially and subsequently at entity functional currency based on fair value of digital currencies at the date of the reporting period, changes in their fair value would be recognised in income statement. Costs incurred in order to generate digital-currencies would be recognised directly in income statement. Digital-currencies maintain in custody would not be recognised on balance sheet excepting by liabilities assuming for entities for losses suffered while custody services are provided.

NIF D-1 'Revenue from contracts with customers'. Measurement, accounting recognition, presentation and disclosures of income from contracts with customers. The recognition of the income is based on the transfer of control of services or products provided by the entity, obligations to comply with customers, allocation of the transaction price and collection rights.

NIF D-2 'Costs for contracts with customers'. Measurement, accounting recognition, presentation and disclosures of expenses from contracts with customers (such as incremental costs to obtain a contract and costs to fulfil a contract).

NIF D-5 'Leases'. New standard eliminates the classification of leases between 'financial' and 'operating' for lessees. One single accounting approach is provided for lessees in which a right to use should be recognised as assets and the present value of leases obligations as a liability. There is an exception in the standard to apply the accounting treatment aforementioned for leases in which the contractual term is until 12-months or where assets related to lease agreement are considered with a low value (no threshold is provided by CINIF therefore it would be determined by each entity considering a materiality assessment). No relevant changes for lessor perspective are included.

On 13th March, 2020, CNBV has issued in Official Gazette changes in particular accounting standards applicable to Financial Institutions including in Annex 33 to match with the adoption of new NIF:

Loans and receivables:

- For measurement of loans and receivables under Hold to Collect Business Model which meets Solely Payment of Principal and Interest test, financial institutions must be used effective interest rate method excepting for those loans and receivables with variable interest rate.

- Implementation of stages in financial assets according to expected credit losses category (Stage 1, Stage 2 and Stage 3).

- New standard methodology to determine expected credit losses 'ECL'.

Financial negative impacts originated by adoption of the new standard methodology for ECL would be recognised either immediately or on deferral basis in following years (12 months) in 'Retained Earnings' category in share capital. In case that negative impacts were greater than 'Retained Earnings' balance, the difference should be recognised in income statement.

On the other hand, if adoption originates positive impacts, they should be recognised as a creditor movement in expected credit losses account in income statement.

- An option to adopt an internal methodology to determine expected credit losses which must be aligned with NIF C-16 'Impairment of financial instruments held to collect principal and interest'.

- Changes in regulatory reporting.

Leases:

There would be a practical expedient for those Financial Institutions that already adopted lease accounting standard for purposes to report their financial information to their holdings since 2019. There would be a recognition of the difference between amounts originated by the adoption of NIF D-5 according to accounting changes provided by CNBV and carrying the amount in lease accounting adopted in 'Retained Earnings' when NIF is in force.

A partial retrospective adoption of these changes whose initial impacts should be recognised in 'Retained Earnings' category in share capital unless there is a different indication or it is impractical.

Revocation of some particular accounting standards applicable to Financial Institutions:

Due to adoption of new NIF, the following particular accounting standards would be replaced:

Particular Accounting standard issued by CNBV to be superseded	NIF in adoption
A-3 General accounting rules applicable to offsetting	NIF B-12 'Offsetting of financial assets and liabilities'
B-2 Investment in financial instruments.	NIF C-2 'Investment in Financial Instruments'.
B-5 Derivatives and hedge relationship.	NIF C-10 'Derivatives and hedge accounting'.
B-11 Collection rights.	NIF C-20 'Financial instruments hold to collect principal and interest'.
C-1 Recognition and derecognition of financial assets.	NIF C-14 'Recognition and derecognition of financial assets'
C-3 Related parties.	NIF C-13 'Related parties'.
C-4 Operating segment information.	NIF B-5 'Operating segment information'.

On 4 December, 2020, CNBV issued in official gazette the adoption date of both NIF and Annex 33 changes aforementioned, which will be 1 January, 2022.

At the end of reporting period, Grupo Financiero HSBC has identified the impacts originated by the adoption of NIF and Annex 33 changes. The process of implantation is ongoing in accordance with timelines agreed.

IV. Accounting recognition of additional loan impairment allowances originated by Covid-19.

At the end of 2020, HSBC booked additional loan impairment allowances of MXN2,038m for Consumer and Mortgages and MXN1,388m for Corporate loans, on top of the methodological reserves. Additional loan impairment charges were originated by:

- *Consumer, mortgages and SME commercial loans* - Some credit exposures have not properly reflected the expected credit losses through the current methodology to calculate the allowances given the skip payments granted as part of the benefit programme.

- *Corporate loans* - The information used to calculate the probability at default of borrowers in certain economic sectors highly affected by the Covid-19 pandemic, was based on their financial information from December, 2019 (latest available) which was not capturing the expected credit impairment given the severe economic situation during 2020.

The release of additional loan impairment allowances will occur once the borrowers show ability payment in accordance with accounting standards issued by CNBV (generally after three consecutive monthly payments of principal and/or interest), the economic pandemic negative effects have been included in the methodology to calculate the allowances or the pandemic risk has been mitigated. At the end of the reporting period, the amount of release is MXN2,651m remaining an additional loan impairment balance of MXN775m.

V. Special accounting rules issued by National Banking Commission applicable to borrowers affected by natural disasters occurred during the period of 29 October and 31 December, 2020.

On 25 November, 2020, the CNBV issued temporary special accounting rules (official response paper No. P-481/2020) ‘the programme’ applicable to borrowers affected by natural disasters occurred from 29 October to 31 December, 2020, as long as, their home address or the cash flows to pay the loans are located or originated in affected municipalities, cities, and states along Mexico that were declared by the Mexican Government as a disaster zone in the Official Gazette.

These special accounting rules are applicable to consumer, mortgages and commercial loans that were classified as ‘performing loans’ at the disaster date according to CNBV accounting standards, as long as the borrower adhered to ‘the programme’ during 120 days after the disaster date.

Basically, ‘the programme’ provides skip payments of capital and/or interest or other type of temporary modification to original terms for a period no longer than three months (excepting by ‘microcreditos grupales’ and agriculture or rural loans in which case the period would be no longer than 6 months or 18 months respectively). Under ‘the programme’ loans modification would not be considered as restructured loan under CNBV accounting standards and they should be marked as ‘performing loans’ during the benefit period.

Providing these benefits, financial institutions could forgive amounts recognised in balance sheet in order to provide more liquidity to borrowers, in which case financial impacts would be recognised against loan impairment allowances already booked or directly in income statement as appropriate. financial institutions could defer on straight-line basis the recognition of loan impairment charges during 12 months.

Although, HSBC applied this programme, at the end of reporting period no loans were adhered to.

Differences between Mexican GAAP and International Financial Reporting Standards (IFRS)
Grupo Financiero HSBC

HSBC Holdings plc, the ultimate parent of Grupo Financiero HSBC, reports its results under International Financial Reporting Standards (IFRS). Set out below is a reconciliation of the results of Grupo Financiero HSBC from Mexican GAAP to IFRS for the first six months ended at June 2021 and an explanation of the key reconciling items.

Figures in MXN millions	30 Jun 2021
Grupo Financiero HSBC – Profit / (loss) before tax under Mexican GAAP	**7,008**
Differences arising from:	
Valuation of defined benefit pensions and post-retirement healthcare benefits, including post-employment benefits	132
Deferral of fees received and paid on the origination of loans and other effective interest rate adjustments	(2)
Loan impairment charges and other differences in presentation under IFRS	315
Recognition of the present value in-force of long-term insurance contracts	(237)
Other insurance adjustments[1]	(308)
Fair value adjustments on financial instruments	431
Deferred profit sharing	(115)
AT1 Valuation[2]	0
Others	52
Profit / (loss) before tax under IFRS	**7,276**
Add back significant items	517
Adjusted profit / (loss) before tax under IFRS	**7,793**
Significant items under IFRS:	
-Debit valuation adjustment on derivative contracts	**(12)**
-Costs to achieve	**(505)**
-Profit / (loss) before tax under IFRS[2]	**US$366m**

[1] Includes technical reserves and effects from Solvency II
[2] Banxico rate at 30 June 2021 MXN19.9062. As of Dec 2020 Banxico rate was MXN19.9087

Summary of key differences between results as reported under Mexican GAAP and IFRS

Valuation of defined benefit pensions and post-retirement healthcare benefits, including post-employment benefits

Mexican GAAP

The present value of Defined Benefit Obligations 'DBO' (including indemnity benefits for other reasons that restructuring), are calculated at the reporting date by the schemes' actuaries through the Projected Unit Credit Method using a corporate/governmental bond rate as a base rate to determine the discount rate applicable.

The net costs recognise in the income statement mainly comprises the current service cost, plus the unwinding of the discount rate on plan liabilities, less the expected return on plan assets. Actuarial gains and losses comprise experience adjustments (the effects of differences between the previous actuarial assumptions and what has actually occurred), as well as the effects of changes in actuarial assumptions. According to Mexican Accounting standard, actuarial gains and losses could be: 1) recognised separately in 'shareholders' Other Comprehensive Income in the bank's consolidated financial statements' and recycling through P&L over the average working life of the employees or 2) totally recognised in income statement.

Modification of plans are recognised in the early date between 1) immediately when the change takes place or 2) when the restructuring costs or indemnity benefits have been recognised.

Given that in 2015, the Mexican accounting standard related to Employee Benefits (*NIF D-3 Beneficios a los Empleados*) changed as part of converge process with IAS 18 Employee Benefits, the Mexican Banking Regulator issued some reliefs in order to recognise initial financial impacts from adoption prospectively over the following five years. Under reliefs' rules, financial impacts from plan modification would be recognised in retained earnings and actuarial gains/losses would be recognised in Other Comprehensive Income progressively over the relief term. Only, actuarial gains/losses would be recycling in income statement over the average working life projected of the employees in accordance to NIF D-3.

IFRS

The main differences between Mex GAAP and IFRS comprise:

1) For Group purposes, the measurement of the present value of DBO is based on a Mexican governmental rate bond, instead of a corporate rate bond.

2) There are not included in DBO the indemnity benefits given that they are not considered as part of benefits granted from past services.

3) Actuarial gains/losses are recognised in OCI under IFRS not subject to be recycling or recognise totally in income statement.

4) Reliefs issued by Mexican Banking Regulator are not applicable to the preparation of IFRS financial information.

Deferral of fees paid and received on the origination of loans and other effective interest rate adjustments

Mexican GAAP

The commissions charged to the borrower at loan inception are recorded into a deferred credit account (liability), which will be deferred against interest income in income statement on straight-line basis during contractual life of loan, excepting by those loans regarding to revolving credit facilities in which the deferral period is twelve months. In the case of commissions charged to borrowers for restructuring or renewals loans, they must be accumulated to the outstanding balance of commissions from original loan and deferring in interest income using the straight-line method during the new term of the loan.

On the other hand, for incremental costs incurred in loan inception, they are recognised as an asset, which is amortised on straight-line basis over the contractual life of the loan as interest expense in income statement.

Both commissions charged to borrowers and incremental costs incurred in loan inception, are recognised in separately accounts in balance sheet, i.e. they are not considered as part of amortised cost of the loan to presentation purposes.

IFRS

After initial recognition, an entity shall measure the loan at its amortised cost using the effective interest rate 'EIR' method.

The amortised cost of the financial instrument includes any premium discounts of fees paid and or received as result of the recognitions of the financial asset.

The effective interest rate is the rate that exactly discounts estimated future cash payments of the financial asset through its expected life.

Given the technical complication in core systems to apply a pure EIR method, HSBC Mexico decided to use as a proxy of EIR the amortised cost indicated for Mexican Banking Regulator, which use the straight-line basis to defer/amortise initial commission charged to borrowers/incremental costs paid to the origination of the loan.

Loan impairment charges and other differences in presentation under IFRS

Mexican GAAP

Loan impairment charges are calculated following the rules issued by the Mexican Ministry of Finance and the National Banking and Securities Commission. Such rules establish methodologies for determining the amount of provision for each type of loan.

Cash recoveries from written-off loans and the positive excess of loan impairment charges are recognised in Loan Impairment Charges in the income statement.

IFRS

The impairment requirements under IFRS 9 are based on an Expected Credit Losses ('ECL') concept that requires the recognition of ECL on a timely basis and forward-looking manner. ECL is determined via a two-step approach: 1) where the financial instruments are first assessed at inception regarding to for their relative credit deterioration, and 2) on ongoing basis followed by the measurement of the ECL (which depends on the credit deterioration categories). There are four credit deterioration categories:

i. Credit-impaired (Stage 3)
ii. Purchased or originated credit-impaired ('POCI')
iii. Significant increase in credit risk (Stage 2)

iv. Stage 1 (the rest of the financial assets in scope not falling into any of the above categories).

Financial instruments with status of ‘performing’ are considered in ‘Stage 1’. Financial instruments which are considered to have experienced a significant increase in credit risk are in ‘Stage 2’. Financial instruments for which there is objective evidence of impairment (in default or credit deterioration) are in ‘Stage 3’. Financial instruments that are credit-impaired upon initial recognition are POCI, remaining this category until derecognition.

Fair value adjustments on financial instruments

Mexican GAAP

Mexican GAAP requires that for those Derivatives and Investment in Securities required to be fair valued, valuations shall be obtained from prices or application of internal valuation models, applied consistently among the operations with same nature.

Inputs for Internal valuation models such as interest rates, exchange rates and volatilities as well as prices used to valuate positions shall be obtained from authorised price vendors approved by Mexican Banking Regulators.

IFRS

Fair Value Adjustments (‘FVAs’) are applied to reflect factors not captured within the core valuation model that would nevertheless be considered by market participants in determining a market price.

Deferred-profit sharing (PTU diferida)

Mexican GAAP

Accounting standards requires that a Deferred-Profit Sharing ‘DPS’ shall be calculated applying a similar model to deferred income tax (assets and liabilities method). It is derived from temporary differences between the accounting profit and income to be used to calculate the profit sharing. An asset or liability for the DPS would be recognised according to method of comparing assets and liabilities sets out in Income Tax standards applicable in Mexico (*NIF D-4 Impuestos a la utilidad*).

IFRS

DPS asset or liability is not allowed to recognise under IFRS.

Present value of in-force long-term life insurance contracts

Mexican GAAP

Mexican GAAP criteria does not recognise this concept, hence do not exists for local purposes.

IFRS

This concept is an intangible asset, referred to as ‘PVIF’ and reflects the present value of the equity holders’ interest in the issuing insurance companies’ profits expected to emerge from insurance contracts in force written at the balance sheet date. PVIF considers insurance contracts in force that are classified as long-term insurance business or long-term investment contracts with discretionary participating features (‘DPF’).

PVIF is determined by discounting the equity holders' interest in future profits expected to emerge from business currently in force using appropriate assumptions in assessing factors such as future mortality, lapse rates and levels of expenses, and a risk discount rate that reflects the risk premium attributable to the respective contracts. The PVIF incorporates allowances for both non-market risk and the value of financial options and guarantees. The PVIF is presented gross of attributable tax in the balance sheet and movements in the PVIF asset are included in 'Other operating income' on a gross of tax basis.

Insurance liabilities and Insurance premiums recognised on an annualised basis

Mexican GAAP

Insurance liabilities are determined based on Solvency II methodology established by local regulator (CNSF) which considers best estimate liability and a risk margin concept. The best estimate is based on up-to-date credible information and realistic assumptions and aims to represent a total liability valuation aligned to its expected pricing transfer to the customer. The risk margin is calculated as the cost of providing an amount of capital equal to 10% of the Solvency Capital Requirement necessary to support the insurance obligations over their lifetime.

Insurance premiums are recognised under annualisation criteria which is based in determine the total premium for the coverage period (one year), consequently total premium is recognised since the moment where insurance contracts are written.

IFRS

IFRS reserving process is based on a liability adequacy test to ensure that the carrying amount of liabilities is sufficient in the light of estimated future cash flows defined by a prudent, non-market consistent set of rules for such estimated cash flows (instead of using realistic assumptions) and not using risk margins components.

For Annuities business there is a securities valuation reserve, 'Reserva para Fluctuación de Inversiones', which is required specifically by CNSF, however, this reserve does not meet MX GAAP criteria nor IFRS to be considered as a liability, therefore this reserve is cancelled for IFRS purposes and recognised into retained earnings.

IFRS criteria does not recognise annualisation insurance premium concept, hence annualisation effect it is cancelled for IFRS purposes

Perpetual Subordinated Debt – AT1

Mexican GAAP

The perpetual subordinated debt is considered as compound financial instrument, i.e. principal meets financial liability definition while coupon of interest meets equity definition given the discretionary in its payment by the issuer according to 'NIF C-11 Share Capital' and 'NIF C-12 Financial Instruments with liability and equity features'. Based on this, principal is measured as a financial liability at amortised cost and coupons are accounted as dividends from retained earnings. Given the instrument is denominated in US$, principal is recognised as foreign currency transaction and reported using the closing rate. Exchange rate changes are recognised in income statement. On the other hand, coupons of interest are recognised in equity when holder has the right to receive payment at historical cost (equity is non-monetary item under 'NIF B-15 Presentation of foreign currencies').

IFRS

Considering the features of the instruments, the perpetual subordinated debt (AT1) is measured according to IFRS9 as an equity instrument. As such, equity instruments are not re-measured subsequent to initial recognition. As the AT1 is classified and accounted for as equity, coupons interest payments are accounted as dividends from retained earnings and recognised when the holder's right to receive payment is established. No subsequent gains or losses are recognised in profit or loss in respect of the AT1 during its life. For instruments in a foreign currency which is different to functional currency of the issuer, no retranslation is applicable (equity is a non-monetary item under IAS 21).

Financial instruments impacted by IBOR reform

Mexican GAAP

During this quarter, CNBV issued a statement about the IBOR reform, which indicates that no restructured loan would be originated for changes in terms and conditions, as long as those changes are exclusively originated by the reform requirements, otherwise modifications would be subject to be analysed under current accounting standards. This is similar to Interest Rate Benchmark Reform Phase 2 for IFRS described below, so the expectation is that it would not represent a difference in accounting treatment.

IFRS

Interest Rate Benchmark Reform Phase 2, the amendments to IFRSs issued in August 2020, represents the second phase of the IASB's project on the effects of interest rate benchmark reform. The amendments address issues affecting financial statements when changes are made to contractual cash flows and hedging relationships.

Under these amendments, changes made to a financial instrument measured at other than fair value through profit or loss 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. Instead they 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 applied from 1 January 2021 with early adoption permitted. HSBC adopted the amendments from 1 January 2020.