2011 Interim Results

Presentation to Investors and Analysts

1 August 2011

Douglas Flint, Group Chairman

Good evening from Hong Kong and a very warm welcome to our 2011 interim results webcast and conference call. I'm Douglas Flint, the Group Chairman; with me are the Group Chief Executive, Stuart Gulliver, and the Group Finance Director, Iain Mackay.

We're going to take you briefly through HSBC's encouraging first half performance, hopefully to allow maximum time for your questions. Stuart will start with the highlights, Iain will then run through the financials, and Stuart will finish by looking in more detail at the business performance.

Before I hand over to Stuart, can I just say a couple of words about the geopolitical regulatory situation. It goes without saying that the current geopolitical and regulatory environment remains a challenging backdrop against which to operate and to plan the business.

We're continuing to take our responsibilities very seriously indeed, and are engaging constructively and transparently with national and international efforts to improve financial stability and the resilience of the international financial system.

At the same time, we're emphasizing the need to maintain and protect the supply of credit to the real economy to preserve the growth agenda. The key point we continue to make is that there needs to be an increasingly robust cost benefit justification for reach incremental measure on top of the already considerable aggregate reform program already in place.

For those of you on the webcast, could you take a moment to read the usual cautionary words on your screens. And for the avoidance of doubt, all the dollar figures in the presentation are US dollars unless stated otherwise. Stuart, over to you.

Stuart Gulliver, Group Chief Executive

Thanks, Douglas. We saw an improvement in financial performance in the first half of 2011, and we've launched a range of initiatives to improve capital allocation, to improve cost efficiency, and to grow the business in the right direction. And we've seen an improvement in revenue trends with higher revenues in each of our faster growing regions.

We go into the second half in a position of financial strength, and with capacity to grow. Reported profit before tax increased 3% to $11.5 billion. Earnings per share increased 34% to $0.51 per share. And dividends in respect of the period were 12.5% higher, as we signalled earlier in the year.

On the right-hand side of the slide you can see our key financial ratios. We reported a return on equity of 12.3%, and the cost efficiency ratio for the half year rose, compared to the first half in 2010, to 57.5%, but declined from 59.9% in the second half. Significantly, the cost efficiency ratio in the second quarter was lower than each of the previous three quarters.

Our advance deposit ratio rose to 78.7% from 78.1% at the end of 2010, leaving considerable room for further growth. And we continue to generate capital, strengthening our core Tier 1 ratio to 10.8%.

Now Iain will take you through the financials.

Iain Mackay, Group Finance Director

Thank you, Stuart. I'll start with our headline numbers on a reported basis. There are four points I want to highlight. Profit before tax, excluding changes in the fair value of our own debt, increased by 16% or $1.6 billion to $11.6 billion. Revenue growth in certain key markets, combined with continuing reductions in loan impairment charges, was partially offset by increased costs. Including the unfavourable change in fair value of our own debt, reported profit was up 3%.

Our tax rate benefited from the non-recurrence of significant taxable gain in the first half of 2010, as well as deferred tax assets recognized in the US during the first quarter of 2011.

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Underlying financial performance also improved. PBT was significantly up against both halves of last year, 13% against the first half, and 20% against the second.

On this slide, we've drawn out the notable factors from underlying business performance, taking the income line first.

We've a number of economic hedges in place to manage interest rates and currency characteristics of senior and subordinated debt instruments issued by HSBC Holdings and certain of the subsidiaries. These do not qualify for hedge accounting, and generated adverse changes of $1.1 billion in the first half of last year, and $314 million in the first half of this. Importantly, these have no impact on the cash flow or economic performance.

Following the refinement of our present value of in force assets within our Insurance businesses, we recognized a gain of $243 million in the period.

Turning now to the expense line notable items. These included $611 million of provisions in the UK relating to customer redress programs, mainly PPI. A pension gain of $587 million in the UK as we rebased indexation against the consumer price index, as opposed to the retail price index.

And a $477 million charge against restructuring costs, notably including the impairment of software development costs mainly within suspended One HSBC programmes, amounting to some $270 million. Finally, you can see the effect of the tax items I've already mentioned.

Turning now to one of our major sources of revenue growth. We grew total customer lending by 6%, and lending was higher in all regions, except North America, where we continue to manage down balances in the runoff portfolios, and also saw lower balances in credit cards as customer behaviour changed.

We grew customer accounts by 5% for the Group, with every region recording growth, so our funding and liquidity position remain very strong.

Revenue trends improved; total gross revenues were broadly stable at $35.7 billion, and the mix improved. Revenues from faster growing regions accounted for 47% of the total, up from 42% last year.

The main growth drivers were strong growth in Commercial Banking, where revenues were $819 million, or 12% higher, notably in Asia and Latin America. And higher sales of wealth management products in Retail Banking and Wealth Management, notably in Asia and in Europe.

Revenues were, however, lower in three main areas. The declines that we already signaled in balance sheet management; in credit and rates within global banking and markets following uncertainty in the Euro zone; and the effect of higher write backs and legacy positions within structured credit last year; and from the continued run-off of consumer finance portfolios in North America, as we mentioned earlier.

Loan impairment charges fell by 32% to $5.3 billion, the lowest since the first half of 2006. Most of the improvement was in the US where the run-off consumer finance portfolios benefited from lower balances and improving delinquency. And our Cards business continued to see households deleveraging, evidenced by increased balance pay down and reducing delinquencies.

This slide shows the significant factors behind the 10% underlying cost growth. I've already covered the notable items; much of the increase in staff costs relates to faster growing regions. In many of these markets, which are very competitive, we also experienced quite significant wage inflation.

As noted, we've launched a number of programmes to improve efficiency and capital allocation. These gave rise to restructuring costs in the second quarter, notably in Latin America, United States and Europe.

These cost efficiency programmes are beginning to turn the momentum, as you can see here. In addition to the increased FTE and wage inflation we also recorded a pension credit adjustment in the second quarter, as noted earlier. As a result, while costs rose by 2% against the second half of 2010, the rate of growth slowed markedly. And in the second quarter our cost efficiency ratio of 54.4% was lower than in each of the previous three quarters.

Finally this slide shows the Group's continued capital strength. There was a 6% increase in risk weighted assets, lower than the 8% increase in customer lending on a reported basis. Continued capital generation led to an increase in our core Tier 1 ratio to 10.8%.

Now let me turn it back to Stuart.

Stuart Gulliver, Group Chief Executive

Thanks, Iain. Today I'm going to focus primarily on our first half performance. But first, I'd like to update you on our progress against the strategy that we articulated in May to become the world's leading international bank.

To recap on the strategy, our network covers the majority of world trade and capital flows, and provides access and exposure to faster growing economies, as well as mature economies.

So how do we seek to position our business, given this context? Well, first, within Global Banking and Markets and Commercial Banking we focus on fast-growing markets and their trade in capital flow connections with another, and with selected mature economies.

Second, within Retail Banking and Wealth Management, we focus on the high rates of wealth creation in the fast growing economies, together with the preservation of stores of wealth in certain target mature economies.

And, of course, we continue to run full-scale retail businesses in the UK and here in Hong Kong.

In May, we outlined plans firstly, to deploy capital more efficiently, secondly, to improve cost efficiency and, thirdly, to achieve growth in target markets. We are making progress in all three areas.

First, we have stepped up discipline in capital allocation using our five-filters framework. We've announced the closure of our Retail businesses in Russia and Poland, focusing instead on Global Banking and Markets, and Commercial Banking connectivity. And we've also announced the disposal of three Insurance businesses in the UK, Bermuda and Mexico.

Much more materially, in the United States we have announced the disposal of 195 branches, principally in Upstate New York, and we're progressing the review of our Credit Card business.

Second, we are targeting $2.5 billion to $3.5 billion of sustainable cost savings by 2013. And, since the start of this year, we've begun operational restructurings in France, the UK, the Middle East, the US and Latin America, which will reduce our headcount by some 5,000.

We've also launched detailed plans to reduce the cost of HSBC's global and head office support functions. And we've initiated more efficient business operating models for our Commercial Banking and Retail Banking and Wealth Management businesses.

Third, we are positioning the business for growth. As a management team, we expect to be judged on growth from both profit before tax and return on equity, as well as cost efficiency.

In Retail Banking and Wealth Management we're expanding in key markets with a substantial growth in sales of wealth products across Asia. In Global Asset Management, funds under management reached a record high at the end of this period.

We also grew revenue from cross sales of Global Banking and Markets products to Commercial Banking customers. And indeed, our cross-border referrals between China and the Rest of the World grew by 50%, compared with the same period last year.

Now let's look in more detail at how we're delivering on our targets, and driving growth by business and then by region.

First of all, Commercial Banking. Commercial Banking profits increased by 31% to $4.2 billion, supported by strong lending and, therefore, revenue growth.

We continue to capitalize on our connectivity between developed in emerging markets, growing our trade revenue by 26%. We grew lending fastest in Latin America and Asia in response to customer demand, and we also achieved significant positive jaws in this business. The return on risk-weighted assets was 2.4%.

This slide shows how we are repositioning our Retail Banking and Wealth Management business to capture wealth creation, to grow revenues, and to restructure the Retail business. We've brought together our Personal Financial Services, Asset Management and Insurance businesses under one management team, headed by Paul Thurston. And incidentally, note that we now report Asset Management here, and not in the Global Banking and Markets segment.

We're achieving revenue growth. We saw a notable increase in sales in Wealth Management in Asia and Europe, and strong growth in mortgage lending in the UK, and here in Asia. And we've conducted a strategic review which will result in our exiting from businesses with a poor strategic fit.

Clearly, the substantial increase in profits in the first half reflected improved loan impairment charges across all regions, notably in the USA for now.

Costs rose as we invested in the increased headcount in Asia and Latin America to support business growth. As Iain mentioned, we also took provisions for customer redress in the UK, mainly in respect of PPI. Return on risk-weighted assets in this business was 1.8%.

In Global Banking and Markets, performance held up well against what was a very strong first half in 2010, but profits were down 16%. But they were actually resilient in the face of difficult market conditions, which led to lower revenues in Credit and Rates in Europe and, as we signalled previously, we also saw lower Balance Sheet Management income.

These factors were partially offset by growth in Financing and ECM, Payments and Cash Management, and Equities and Securities Services.

We've often argued our Global Banking and Markets business model is different from our peers, and this can be seen perhaps a little more clearly in the first half of 2011 where we have fared better than others. The diversity of our business was a protection in difficult markets, with revenues from faster growing regions rising by 10%, partially offsetting weaker performance in Europe. Return on risk-weighted assets was 2.6%.

Now let's turn to the regions, starting with Europe. Compared with the first half of 2010, profit before tax fell by 39%, and on an underlying basis it fell by 28% to $2.2 billion. As I mentioned a moment ago, this was driven mainly by a lower contribution from Global Banking and Markets. However, Global Banking and Markets remained strongly profitable in Europe.

In Commercial Banking in the UK, income from customers using International products grew by 16%, and we increased gross new lending to SMEs. We remain on track to achieve our lending goals under the Merlin agreement.

We also continue to grow our mortgage book in the UK. Our mortgage share of new lending rose to 11%, and this new lending is very high quality with a loan-to-value ratio of 53%.

Higher costs in the UK reflected strategic investment in Global Banking and Markets but, since the period end, we have announced a restructuring in the UK and in France, affecting around 1,400 jobs.

In the Middle East and North Africa performance was resilient. We remained open for business, despite unrest in 10 out of the 14 markets where we operate. Profit before tax was significantly higher than the first half of 2010, mainly reflecting improved credit performance, with strong growth in reported PBT in our three largest markets in the region, Egypt, United Arab Emirates, and Saudi Arabia.

Costs were higher, however we announced a restructuring during the period as we focused on improving business efficiency. And as you would expect, revenues remained subdued, due to the uncertain political environment.

However, it's worth remembering this is a region that's home to 60% of the world's oil and to 6 of the 10 largest sovereign wealth funds. And also, we've operated here for more than 50 years, and we therefore remain optimistic about the region's prospects.

In Latin America our pretax profits rose 23% to $1.2 billion. Overall revenues for the region were up 12%, driven by growth in Brazil. We achieved notable revenue growth in Commercial Banking, and Retail Banking and Wealth Management.

We continue to restructure our regional head office to improve cost efficiency, and where we saw cost growth this was reflected by wage increases in the inflationary environment, and also additional front-line staff recruitment, especially in Brazil. The costs also reflected the first tranche of restructuring following the closure of 66 branches in Mexico.

The North American business achieved profit before tax of $672 million, compared with a loss in the same period last year. We continue to manage down the Consumer Finance portfolio, and balances in cards declined. As a consequence, total revenues were lower. This contributed, of course, to the higher cost efficiency ratio, but also to considerably lower loan impairment charges and, therefore, to improved profit before tax.

We continue to reshape our US business. As I said earlier, we've announced the disposal of 195 branches, principally in Upstate New York, and we're progressing the review of the Cards business.

Canada continued to perform very strongly, and was our fifth most profitable country in the first half with a profit before tax of $527 million.

Now at the full year, I emphasized that protecting our leadership position here in Hong Kong was absolutely core to our business in Asia, so it's encouraging to see Hong Kong continue to perform very strongly. We saw balance sheet growth, strong sales of Wealth Management products and mortgages, and an increase in trade-related revenues. I'd also note the continuing strong credit quality. Customer loan balances grew faster than risk-weighted assets as we added good quality lending.

Staff costs rose, both to support increased business volumes, and in response to inflationary pressures.

Profits in the rest of Asia Pacific rose 21% to $3.6 billion. We achieved strong revenue growth of 13% overall which, as you can see, was well spread across our major markets, with particular strength in mainland China. We saw robust lending and deposit growth and widening deposit spreads, and we increased sales of Wealth Management products.

As in Hong Kong, staff costs rose to support increased business volumes, and also reflected inflationary pressures. The contribution from our associates also rose. Together, Hong Kong and the rest of Asia Pacific produced over half of the Group's profits.

Finally, I'd like to say a few words about the economic outlook. We remain positive on emerging markets. We anticipate a soft landing in China, and expect the risks overheating in Hong Kong to ease. We expect continued strong growth in the rest of Asia and Latin America, and we remain positive on the outlook for the Middle East.

But there are clear short-term concerns. The geopolitical and regulatory backdrop is uncertain, and presents challenges for developed economies.

In closing, I would add that I'm pleased with these results which mark a first step in the right direction on what will be a very long journey.

Thank you for your time and attention; we'll now take your questions. First, the operator will explain the procedure and introduce our first questioner. Thank you.

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Questions & Answers

1 August 2011

Sunil Garg, JPMorgan.

Sunil Garg: I just wanted to understand the increase in loan loss provisions in second quarter versus first quarter. From what I understand, North America seems to be behind that increase, despite the decline in delinquencies and charge-offs at HFC, so just wanted some colour on that.

Second, if you could tell us the capital gains that you're likely to book on the sale of the branch network to Bank Niagara today.

And lastly, just some colour on your outlook for the rates, the FX and the Equities businesses in the GBM, which has done very well on a half-on-half basis.

Stuart Gulliver: Iain will take the first two, and then I'll comment on Global Banking and Markets.

Iain Mackay, Group Finance Director

So US gains, Sunil, I'm sorry, your first question was?

Sunil Garg, JPMorgan.

The quarter-on-quarter increase in provisions from $2.4 billion to $2.8 billion.

Iain Mackay, Group Finance Director

Actually, the main driver behind the loan impairment charges, Sunil, is actually in the line of impairments on available-for-sale securities.

We took $65 million against Greek bonds, and then there was some $280 million on other impairments within available-for-sale securities. So that was the main driver in the second quarter. If you think about what was underlying that, it was principally what we saw going on in the Eurozone, so that was it.

If you look at the US portfolio, overall, the loan impairment charges there were stable. Obviously, we've had a declining trend over the last seven or eight quarters in that particular area, and that trend stabilized in the second quarter of the year, although obviously, continued to represent a significant decline against the same period last year as well as the second half of 2010.

As it relates to the transaction in the US, that transaction's priced off the deposits which will be sold to First Niagara when the transaction closes sometime in early 2012.

The premium to those deposits is about 6.67%, and once the transaction closes, it's obviously highly dependent on the deposit base at the time the transaction closes. We'll obviously provide a little bit more insight to certainly the accounting gain that would be generated from that.

In terms of capital release off the risk-weighted assets that are being disposed, it releases about $350 million. And in terms of the overall proceeds, we're going to realize somewhere in the region of $1 billion from the proceeds of that transaction.

Stuart Gulliver, Group Chief Executive

Thanks. As for Global Banking and Markets, I think what you've got to do is dig into the various revenue lines within Global Banking and Markets. Clearly, we are impacted, in line with the market, by what's gone on in Europe, and you can see that in the credit line, which is actually down year on year.

But actually, in rates and foreign exchange, Equities and Securities Services were up, because these are really businesses that are based around customers in the emerging markets. So our Global Banking revenues are up 12%. Equities are up 23%, which is really an Asian business now, with some Middle Eastern and Latin American components. Securities Services is up 14%; Payments and Cash Management's up 24%.

So as we've said often, we have a different mix of revenue streams within this business, and I see no reason why we shouldn't continue to see reasonable growth in foreign exchange in Global Banking, in the equity piece, Securities Services, and PCM.

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Obviously, to our credit, and the fact we're a primary dealer in a number of European government bond markets, that credit line will be impacted if the Eurozone problems continue to resurface and that's chronic.

Remember, we don't have a significant commodities trading business, which is one of the reasons why I think we've outperformed some of the competition. We never built one and, therefore, we haven't seen a strong reversal in earnings that have come through in a number of the FICC numbers of our competitors.

But this reflects a lot of the investment we've made to really develop a customer-facing Global Banking and Markets business. And we're starting now also to see some reasonable traction in ECM and equities here in Hong Kong, which has always been a little bit of our Achilles' heel.

We've always been a very strong debt house in Asia, but had some catch up to do. There's still a lot of catch up to do, but there's at least some trends/directional information here in that area which is also encouraging.

Sunil Garg, JPMorgan.

Got it. Thank you very much.

Ian Smillie, RBS.

Three questions please, all relating to geographic movements on the balance sheet. Firstly, could you give us a sense as to the contribution to the Other Asia risk-weighted assets from the associates?

The reason I ask is that about one-third of the incremental Group RWA uplift is coming from Other Asia, and the RWA to loan ratio there is about 200%, heavily distorted by the associates. So some understanding of the contribution to the number there would be very helpful.

Secondly, inside Europe, if we could understand why the incremental RWA move is so low, given that there's a very big pickup in the loan book there, which doesn't seem to be flowing through to risk-weighted assets.

And then thirdly, inside the strong deposit performance of the Group, it looks like France is the standout geographic contributor. Again, I'm guessing that's coming from GBM, but some colour as to what's happening inside there would be very helpful.

Stuart Gulliver, Group Chief Executive

I'll kick off with France and Europe, and then Iain can talk about the associates. So the deposit base in France is not coming from Global Banking and Markets. It's actually coming from the build out of a Commercial Banking and Retail Banking Wealth Management business there, and a very deliberate policy to reduce the AD ratio of our French business, where the French market traditionally runs with AD ratios of 120%/130% more towards a Group standard. So that's quite a deliberate move on the part of our French colleagues to actually win deposits within that market.

The RWA impact in Europe is probably due to the growth of actually two things; in essence, mortgages in the UK, which obviously carry low risk weights, this is the bit I talked about earlier with the 53% LTV; and also, we've done quite a bit of a switch into secured lending from unsecured lending, so growth in trade finance and so on contribute quite low RWAs.

As for the associates, Iain?

Iain Mackay, Group Finance Director

Well, I'm actually busy searching for that number, Stuart. What I can tell you, Ian, is that what we've done with the risk-weighted assets within the associates and rest of Asia Pacific, in actual fact consistently across the Group that we've allocated them into the customer groups to which they relate.

As far as the Chinese associates go, the most significant proportion of that relates to Commercial Banking, within BoCom obviously, approximately 60% to 70% of the risk-weighted assets, which are consolidated on a proportional basis for regulatory reporting sit within that. I don't have the exact number at my fingertips, but I will get that number to you at a later date if you don't mind, Ian.

Stuart Gulliver, Group Chief Executive

Actually, Ian, if you look at page 29, you can see an illustration of what Iain's talking about. The Commercial Banking RWAs are actually greater than the Commercial Banking's nominals, and that's BoCom, so you can probably make a stab at that yourself.

It's why there's an oddness to the fact that the nominals are actually, in the case of Commercial Banking, lower than the risk-weighted assets; it's because of the attribution of the associates' BoCom numbers into CMB.

Ian Smillie, RBS

That would be great. Thank you. A hard number, a follow-up there would be extremely helpful.

Stuart Gulliver, Group Chief Executive

Yes, we'll follow up with a hard number. As I say, page 29 gives you some directional information.

Ian Smillie, RBS

Great. Thank you. One quick follow-on please. The restructuring charge taken in the half, is that on a pay as you go basis, or is there some degree of forward-looking for the headcount reductions which have been talked about?

Stuart Gulliver, Group Chief Executive

They're pay as you go.

Iain Mackay, Group Finance Director

Absolutely. What's been, if you like, announced in Card at this point, Ian, and that's the way in which we're going to move.

Ian Smillie, RBS

So if there's headcount reductions as they come through, any restructuring charges associated with that will be taken at that time?

Stuart Gulliver, Group Chief Executive

Yes, that's right.

Iain Mackay, Group Finance Director

That's the case.

Ian Smillie, RBS

Great. Thank you.

Cormac Leech, Canaccord

One detailed question, please, and then a slightly broader one. Just on the restructuring charge, you've given us an allocation of that geographically. I was wondering if you could give us a little bit of colour on by-customer group how that breaks out.

And then secondly, I was wondering if you could give some of the reasoning for expecting a soft landing in China. Thanks.

Iain Mackay, Group Finance Director

Shall I take the first, Stuart?

Stuart Gulliver, Group Chief Executive

Yes, sure.

Iain Mackay, Group Finance Director

On the restructuring, Cormac, of the total $477 million that was recognized in the first half, $270 million of it related to impairment on software development costs across a number of suspended work streams within One HSBC. If you'll recall, there were about 10 work streams there. We suspended work on 3 as we revisited the business models for Commercial Banking and Retail Banking and Wealth Management. The total impairment there was $270 million.

Across the remaining $200 million, that was principally restructurings within Latin America, the Middle East and Europe. In Latin America, which was the larger of the three at this point, it's principally within the Retail Banking and Wealth Management space as we restructured some 66 branches within Mexico, but also addressed some of the head office structural matters within Mexico as well. But broadly, within Retail Banking and Wealth Management.

So I think, as we move through this, you'll find that there'll be a spread across the customer groups, and we'll keep you informed as to how that comes through.

Stuart Gulliver, Group Chief Executive

Okay. Turning to China, the slowdown in the economy is part of the policy statement that was made in the 12th Five-Year Plan where China indicated that it wished to see GDP growth drop to around 8%, and that 8% was a sustainable number, and that the 13% number that they'd been peaking at was, in their view, unsustainable and would lead to some social pressures within the country.

So first of all, this was not a slowdown that's being done to the Chinese Government, i.e., it's the economy and they're responding, it's a direct policy initiative of the Chinese Government.

Now because China does not have a fully developed money market, its central bank is not simply reliant on official interest rates, i.e., the Fed funds or base lending rate equivalent, to try and influence the overall macro direction of the economy. It has a raft of micro-prudential levers at its disposal, everything from moving reserve ratios to actually being able to direct through the branches of the State-owned banks, specific lending to specific sectors by city, by province.

So the richness of the micro-prudential tools, and frankly, the technical skills of the technocrats at the center, many of whom I have met and have visited for over actually 25 years, gives me a great deal of comfort that China actually will manage a soft landing, and will not have a hard landing.

Cormac Leech, Canaccord

Okay. Thanks.

Alastair Ryan, UBS

Two, if I may? First, given capital how generative the Group is, how strongly all your key metrics are improving, whether we should be using EPS growth as a proxy for your thoughts about dividend distribution capacity at present, because clearly, one's growing meaningfully faster than the other in the first half.

And then secondly, just a point of interest really: Hang Seng pretty much stepped on the brakes in the first half, and it looks like Hongkong Bank in Hong Kong kept on lending at a pretty fair clip, whether there's anything we should read into the shift there. Whether that's because of the different mixes of the two businesses, but historically, they've often grown in line and actually, quite a big divergence in the first half, what we should read into that? Thanks.

Stuart Gulliver, Group Chief Executive

On Hang Seng Bank, I don't think you should read anything into it other than the different business mixes of the two banks. Don't forget that the Hongkong and Shanghai Banking Corporation came off the pace in 2009 when we were doing the rights issue for the Group overall, and actually scaled back some of its balance sheet growth at a time where Hang Seng Bank did not need to do so.

So to some extent, you need to look at the fact that the Hongkong and Shanghai Banking Corporation underperformed in terms of volume, variant Hang Seng Bank during the period where we raising capital at the Group level.

As for dividends and share price performance and EPS, I don't think we see the world in quite such a rosy way as you do in the following sense. Okay, in the first half, we have an ROE that appears to have got inside our target of 12% to 15%, but, of course, that's based off a Basel II capital number.

If you re-base and recalculate this which, of course, is what we do, based on our estimates of where Basel III would be, that ROE number falls quite dramatically. To put it into context, roughly estimating on a Basel III basis, we'd need to have made an extra $2 billion in the first half, so not $11.5 billion, but $13.5 billion, to have got a 12% ROE on Basel III.

So I think if you're working round to share buybacks, etc., I think we're a long ways away from that and, indeed, were we to get into a situation where we had far too much retained earnings, we'd deal with it through dividends rather than share buybacks. I don't know, Iain, if you might want to add anything else.

Iain Mackay, Group Finance Director

I think the other thing to bear in mind, Alastair, is within that return on equity that we reported for the first half, it's obviously got the benefit on the tax line of a not insignificant credit from the utilization of foreign tax credits through deferred tax recognition in the US.

So if you normalize for that one-time effect, our return on equity comes down to round about 11.5%, 11.6%. And then there's the effect that Stuart talked to in terms of a Basel II versus a Basel III measurement basis.

Alastair Ryan, UBS

Thank you.

Christopher Wheeler, Mediobanca

Three questions, if I may? First of all, just a confirmation on the UK tax, the bank tax. $600 million I think was the number you've been suggesting might be the liability. Can I just confirm that will all come now in the second half, and whether or not you've actually revisited that in any shape or form, given you haven't got a lot more information? That's the first question.

The second one, a follow-up restructuring; obviously, we are going to see some pretty hefty restructuring charges, one must assume, over the next 2.5 or 2 years or so. Again, can you give us any thoughts on perhaps what you can share with us on the sheer scale of those on a half-by-half basis? And whether the $477 million is a reasonable guidance as to where we might be, albeit I know you had the software charge there. And yes, those are the two questions. Thank you.

Iain Mackay, Group Finance Director

Okay. Chris, I think on the bank levy, as you quite rightly point out, there's no new information on that front. So I think, as you leaf through, with great delight, the 250 page document that we provide, you'll find that our disclosures on that regard are consistent at $600 million.

The accounting for this is still rather odd, in the sense that we would theoretically book the whole thing on December 31, once we know the shape of the balance sheet on that day. But no, the number has not changed.

On restructuring charges, I wouldn't read too much into the first half. As we implement around sustainable saves and consistent business models across Retail Bank and Wealth Management, as that may or may not affect headcount, as it may or may not affect other items, whether it's in the form of dispositions or closures of businesses, we're absolutely going to try and balance the overall natural attrition that we see coming through headcount on an annual basis, in terms of how we right size the workforce in each of the key regions around the Group, and try and effect that in as efficient a way as possible.

So I certainly wouldn't read too much into the $477 million or, for that matter, the $200 million excluding the software charge.

What we absolutely will do is, as we have clarity on each on the measures that we're implementing, we'll provide you with that information on a timely basis.

Christopher Wheeler, Mediobanca

Thank you very much.

Leigh Goodwin, Citigroup

A couple of questions, one on Balance Sheet Management; the other one on the US Finance Corporation.

Just on Balance Sheet Management, it came in at $1.8 billion, just under, for the half. It looks a little bit stronger than perhaps your previous guidance for the full year of $2.5 billion would imply. I wonder whether you could give us a Q1/Q2 breakdown of that. And also, whether you want to take the opportunity to amend your guidance for the full year.

And on the US, my question is that it looks like the impairment charge ticked up. If you take out the first quarter $400 million special provision for the change in economic assumptions, it looked as if there was an increase Q on Q of about $200 million.

And the delinquencies on the secured books look as if they've got up a little bit. I just wondered whether you could talk about trends in the US as well then please. Thank you.

Stuart Gulliver, Group Chief Executive

Okay, I'll do the Balance Sheet Management, Iain the delinquency trends.

We have unexpectedly, I guess from our original assumptions, seen higher interest rates in a number of the countries in the rest of Asia Pacific in response to higher inflation. Actually, it's also true in Latin America.

So actually, we've seen interest rates go back up and actually seen quite steep curvature in the yield curve in Latin America and in the rest of Asia Pacific, which has benefited our Balance Sheet Management numbers.

We've also seen at times in the UK, and at times also in the Eurozone, where obviously, rates are going back up, opportunities, if you like, to reload our positions where one and two year rates have backed up to a level against the overnight carry rate.

So I think it probably would be appropriate to lift that Balance Sheet Management guidance where I think we've set the expectation around $2.5 billion to $2.5 billion to $3 billion, but probably not higher than that because, actually, a lot of the curves again, particularly in the Eurozone, sterling etc., have gone back to being incredibly flat and the extent to which we've seen rates rise in the emerging markets, so it's already happened as it were. But I do think the $2.5 billion to $3 billion number rather $2.5 billion is more appropriate.

Iain Mackay, Group Finance Director

Talking to loan impairments, certainly when you look at the US books of business, whether in the context of 2+ delinquency, continued downward trend in delinquencies across the Mortgage Services portfolio which, as you will recall, has been in runoff now since really the first quarter of 2007, and as it relates to the Consumer Lending portfolio, which has essentially be in run-off since the tail end of 2008, absolutely stable quarter on quarter.

Loan impairment charges in the US, as you quite rightly pointed out, in the first quarter, we took an adjustment for some of the economic assumptions, primarily related to foreclosures in that regard. But in the second quarter, they've actually dropped off, again resuming that downward trend that we'd experienced in previous quarters.

Perhaps if you look more broadly at loan impairments across the Group, one of the effects that you may be picking up is slightly higher impairments on the Available-for-Sale portfolio in the second quarter, as we took the effect of impairments on Greek Government bonds, which was $65 million. And then the effect of some repricing within the Available-for-Sale portfolio, which took us to about another $280 million of impairments in the second quarter.

So that may be the factor that you're picking up there.

Leigh Goodwin, Citigroup

Very good, thank you.

Mike Trippitt, Oriel Securities

Two or three questions, if possible. Stuart, you mentioned the 5,000, I think, job cuts on the restructuring so far. What I'm trying to do is just marry up the potential headcount reductions. I've seen different figures mentioned; I'm not sure that some of those are officially in your disclosure or just on the wires, but of more like 25,000. I'm just trying to match up the headcount reductions against the $2.5 billion to $3.5 billion of cost saves that you see over the next two or three years. I wonder if you could clarify that.

Secondly, looking at the 10Q for Household, you're still about the $6 billion level on the capital. And I'm just wondering, is there any pressure to increase that? Or how does that capital move as you continue to run-off the balance sheet?

And the third thing is, there's an FX benefit in the core Tier 1. And I'm just wondering, are you naturally hedged in terms of risk assets and core Tier 1? Or is there any real benefit to the core Tier 1 ratio from that FX effect?

Stuart Gulliver, Group Chief Executive

Let me start with the jobs. We've confirmed that there are 5,000 job cuts that took place in the first half, which were made up of 700 in France, 700 in the UK, 1,700 in Latin America, 1,400 in the United States, which is totally separate from any disposals, and 300 in the Middle East.

What we've also said, and I said it in answer to some questions earlier today, is that I expect to make a further 25,000 job cuts between now and the end of 2013. These are in addition to the 5,000, so a total of 30,000.

This is a very approximate ratio, but if we're looking to take 10% out of the cost base of the firm, it's not altogether surprising that it's about 10% of the headcount of the firm.

What I've also said though, Mike, is that these are gross numbers. So therefore, given that we are in parts of the world that continue to boom, it is quite possible that the net headcount number is not minus 30,000.

It could be a smaller number, because we've added people. It could also be a bigger number because we've been successful in disposing of businesses, because this headcount cut do not include headcount that leaves the firm as a result of selling a business.

Mike Trippitt, Oriel Securities

Thank you, that's very clear.

Iain Mackay, Group Finance Director

As it relates to capital in the Finance company, as we run down the portfolio, as you would quite naturally expect, there would be some release of capital as we reduce those risk-weighted assets.

However, at the same time, there are some changing characteristics in the portfolio with respect to either probability of default, or loss given default, there is some upward pressure in terms of risk-weighted assets in that regard.

But overall, the Finance company is capitalized at a level with which our supervisors are happy, to the extent that we release capital as we run down those portfolios. That capital will be released, certainly within the North American environment, for redeployment across other lines of business, in terms of being able to distribute it from North America back to parent for allocation elsewhere, that’s somewhat at the gift of the US supervisor at this point. And as is well documented in the press, the US supervisor is less inclined to allow banks to do such things. But overall, certainly, we're at the level or above the levels of capital with which the US supervisors are happy at this time.

In terms of the FX effect on the capital ratios, specifically speaking, we're generally hedged across our subsidiaries and branches, just by the composition of the balance sheet, which tend to be naturally matched in the currencies within the businesses in which we're doing work.

So we don't carry significant unhedged positions within the capital base. And generally, the capital base is not that susceptible to significant movements within our businesses.

Mike Trippitt, Oriel Securities

So the core Tier 1 and the RWAs would have moved in a lock step, so there shouldn't be a benefit to the Tier 1 ratio itself?

Iain Mackay, Group Finance Director Not significantly. There are some structural FX positions that we hold but, generally speaking, it's largely matched.

Mike Trippitt, Oriel Securities

Thank you.

Tom Rayner, Exane BNP Paribas

Could I just ask you about the seasonality in the cost income ratio quarter by quarter because, obviously, the second quarter things look a lot better than first quarter? But if I look at the first half and first half trends, even adjusting for numerous one-offs and the US run-off, revenue was pretty flat; costs were high single digits. So it's going the wrong direction at the moment, despite pretty good volumes and, I think, a better BSM outturn in the first half.

So I just wondered if you could give us any thoughts on whether the move into the second quarter is more reflective of what's really going on, or are we going to have to wait a bit longer, possibly, for the improvements to come through? Thank you.

Stuart Gulliver, Group Chief Executive

The second quarter, I think, is probably more directionally indicative of the journey we're on. Don't forget, we only had the investor day on May 11. The new team took over on January 1; this 300,000 roughly staff in 87 countries is quite a large ship to turn.

What's quite pleasing within the first to second quarter numbers is there's a strong revenue growth actually in Commercial Banking and Retail Banking and Wealth Management, so actually, the revenue line actually picked up first to second quarter. And I think looking around at some of the comparative results reporting so far, that's actually quite unusual.

But I'll let Iain just comment on any of the technical cost numbers that are running through that. Clearly, as you'll appreciate Tom, there's a raft of one-offs flowing through these numbers.

Iain Mackay, Group Finance Director Yes, Tom, I have great fun trying to explain our cost number, just because of all those one-offs. But I think, obviously, the focus for the business over the last few months has clearly been delivering against some of the sustainable cost savings that we laid out in the strategy day at the beginning of May.

We're clearly beginning to build some momentum in that regard; we would expect to continue to build that and deliver on some of those sustainable saves through the second half of the year. But as Stuart quite rightly points out, there are a number of programs that we've got underway in this regard.

We're certainly on a good trend, but there are some vagaries, if you like, in some of the revenue lines that we saw in the second quarter, certainly with respect to some uncertainty in the European area, which we'll keep a very close eye on, and then adjust course within the cost lines as we see the revenues coming through.

But momentum's good and I think, generally, we're on the right glide path to get to the cost position that we want within the Group.

Tom Rayner, Exane BNP Paribas

Thanks for that. Could I just have one quick follow-up, unrelated, just on the impairment you've taken on your Greek bond exposure, what percentage of the gross exposure did that represent?

Iain Mackay, Group Finance Director

I think, against the carrying values that we had at June 30, it was just over 30% in the Available-for-Sale portfolio and (multiple speakers).

Tom Rayner, Exane BNP Paribas

And would that have been marked down to market levels?

Iain Mackay, Group Finance Director

Yes, it ran to about 30% deduction against available-for-sale within the Greek bond portfolio at that time, so it was round about $200 million at that time.

Tom Rayner, Exane BNP Paribas

Okay. Sorry, the carrying value that would have been mark to market already, and then you've taken in a 30% impairment on top of that, or that's the total impairment?

Iain Mackay, Group Finance Director

No, that's the mark to market, okay. So we, in effect, mark to market in available-for-sale security at June 30.

Tom Rayner, Exane BNP Paribas

Okay, thank you.

Rohith Chandra-Rajan, Barclays Capital

A couple, if I could please? One on operating trends, and a couple of slightly related actually on broader strategic issues.

Just on the operating trends, you signalled at the 1Q IMS that you were looking at margin stability. Margin, for the first time in a number of years, seems to have improved in the quarter, so up from 252 I think in the first quarter to 256 in the second.

You talked previously about stabilization, certainly on the deposit side, in terms of liability spreads, I wondered if you could give a bit more colour as to how you think about the margin, going forward?

And then secondly, more broadly on the strategy, you highlight in the statement progress on the strategic review of the Credit Card business in the US, that obviously handles about $60 billion of RWA, so much more significant versus the $350 million of equity that you highlighted in the branch disposals, and so I wonder if you could give a bit more colour around that?

And also, coming back to your comments on costs, I'm just wondering in terms of initiatives that you've announced so far, how far in terms of run rate that might get you to the $2.5 billion to $3 billion of targeted cost reduction? Thank you.

Stuart Gulliver, Group Chief Executive

Okay on net interest margin, there's a number of moving parts in the net interest margin number. We continue to run down that very heavy margin business in the States, Household, which obviously has resulted in the contraction of net interest margin. But in the other direction, we are starting to see actually the ability to re-price credit, actually in places like Hong Kong and China because interest rates and reserve ratios have increased a number of times.

On the other hand, in the rest of Asia Pacific we're again seeing deposit margin increases as interest rates have gone up in a number of countries; same in Latin America. But here in Hong Kong, there's actually deposit compression, partly caused by a significant amount of money having moved into RMB out of US dollars and Hong Kong dollars creates a little bit of a kind of shortage in those currencies. And in the UK, there's also deposit margin compression coming out of the competition for deposits from the state-owned banks looking to repay the special liquidity scheme of the Bank of England by December of this year.

So it's reasonably mixed, but the encouraging bit is that we're actually starting to see some ability to re-price credit across the piece in Asia Pacific.

So there are some signs of everything balancing out. Again, just on the negative, we have deliberately started to move the book into secured from unsecured; that, of course, has a lower outrun rate.

On the strategy, we've got nothing to report today on the Credit Card portfolio in the United States, other than that the process continues to run. Once we have got something to report, we will come back to you all at that point in time and, yes, you're entirely correct that this one is the one that has a material amount of RWAs and would make a material difference in terms of capital release, but it's a work in progress at this moment.

As for the costs, I think we're only in the foothills of the restructuring that's required to deliver the $2.5 billion to $3.5 billion; there's a lot more to come.

Rohith Chandra-Rajan, Barclays Capital

And I guess your comments earlier just on the costs; the 10% headcount reduction is consistent with the 10% reduction in the cost base. Is that the case based on the 5,000 to date, would that be a fair assumption?

Stuart Gulliver, Group Chief Executive

No, that's based on the 30,000, the 25,000 plus the 5,000.

Rohith Chandra-Rajan, Barclays Capital

Sorry, so if I use the same assumption based on the 5,000 to date versus your comments on the 30,000?

Stuart Gulliver, Group Chief Executive

Yes. Clearly, I think the thing to understand is I'm not managing to a headcount target; I'm managing to a cost efficiency ratio target that we set out.

Remember when we set out the sustainable cost saves, we also did not say that you'd be able to deduct $3.5 billion from the cost base of $37.8 billion and find that we were operating at $34 billion, it was to create capacity.

Equally as we remove a chunk of jobs, we're clearly going to try and remove the biggest amount of cost we can. So it's not really about headcount, but the headcount has become a focus for a number of the press commentators in the last 48 hours.

But it would be fair to say that one of the significant inputs to that $2.5 billion to $3.5 billion, but only one, is clearly a reduced headcount.

The other thing to bear in mind about this is the 25,000 plus 5,000 takes no account of what the ICB may require us to do or, indeed, we may decide to do as a result of whatever the ICB recommends.

And again, it's impossible for us sitting here this evening to say whether that would result in a reduced headcount beyond the 30,000, or actually an unchanged headcount.

Rohith Chandra-Rajan, Barclays Capital

Okay, thank you. And I appreciate you highlighted the uncertainties around all the number of different drivers around the margin. Is your expectation still stability, going forward?

Stuart Gulliver, Group Chief Executive

Yes, I think it is actually. Don't forget, we have got this big portfolio running down and also, if we are successful in selling that Credit Card business, that's clearly a very high margin asset business, so you also need to factor that in.

In a way, the net interest margin of the Group has been flattered by a couple of businesses, one of which actually had a very high revenue number, but an extremely high loan impairment charge and write-off number and, therefore, a disappointing PBT. The other, which has had a high return and actually a very profitable experience for us, but which is non-strategic.

So don't forget, if we do succeed in disposing of the Credit Card business, it will be negative for the net interest margin at kind of first blush, but it's not a business that strategically makes sense for us. And we think if we're able to do that and release a chunk of capital, we would do much better by our shareholders to redeploy that into faster growing emerging markets in assets with much lower risk weights than where it currently sits.

Rohith Chandra-Rajan, Barclays Capital

Okay. Thank you very much.

Michael Helsby, Bank of America

I've just got a few questions, if I can? Firstly, on loan growth, across the regions I think you've seen a slowdown as you flagged in Q1 in the first half versus year on year. I know you've got quite a bullish outlook on emerging markets, soft landing in China etc., I was wondering if that level of growth now has reached a level that you feel quite comfortable with, so you're quite happy with that type of balance sheet growth from a risk appetite whilst you look forward?

And second question on volumes and trading; I was wondering if you could give us any comments if you've seen any contagion or disruption in the market in Asia as a result of all the noise that you're seeing coming out of the US and out of Europe?

And attached to that really, but just thinking more about your Fixed Income businesses, I was wondering if, in a developed market perspective, whether you can relate to the revenue declines that peers have been seeing, so in FICC people have had down mid 20s Q on Q? I appreciate you've not got the same business mix.

Stuart Gulliver, Group Chief Executive

In terms of loan growth across Asia Pacific, we are reasonably comfortable with the loan growth that we've seen. We have not in any way loosened our credit underwriting standards, and we're comfortable with the credit risks that we're taking.

We continue to have a very low advanced deposit ratio; we continue across Asia Pacific to have an AD ratio of 59%; we have a lot of liquidity; we've grown our deposit base as well as grown our loan growth.

The RWA growth in Asia was about 8.5%; the loan growth was about 13%. So we're booking good quality and assets, so we're comfortable with these kind of run rates.

I see no real impact from what has gone on in the United States and what's gone on in Europe to our business in either Latin America, the Middle East or, indeed, Asia Pacific. And that, of course, explains in a large part why our Global Banking Markets business is down 16% and others are down by much more. We have a very different business model; it's must less proprietary trading; we've never built a commodities business up so we don't have the now negative swing of a commodity business.

And we have a business that's very much rooted in a customer base, and in a customer base where GDP growth is very high. Asia, ex Japan, GDP growth we forecast at 7.5% in 2011. That's obviously much higher than where Western Europe, the UK, or the USA sit.

So I think what would be fair to say is if you look at our credit business in Europe, which is the biggest like-for-like read across to where we're a European primary dealer, we do have similar declines in our profitability to what you've seen other European primary dealers have.

But as I say, that's quite a small proportion of the Global Banking Markets business. It's really been built around seven or eight revenue streams, all of which make over a $1 billion, and is geographically diversified to the emerging markets.

Michael Helsby, Bank of America

Okay, thank you.

John Kirk, Redburn Partners

I've just got one question actually or one area, which is in Hong Kong, and particularly on this issue of Hong Kong dollar liquidity tightening up. Could you just give us your view on what that could mean for Hong Kong margins, going forward, and also whether you think that could end up constraining Hong Kong loan growth?

And then finally, whether actually, given your quite low L/D ratio in Hong Kong, whether that is a Hong Kong dollar L/D ratio, but also whether that would put you at some sort of competitive advantage if Hong Kong's dollar liquidity continues to tighten?

Stuart Gulliver, Group Chief Executive

I think there's actually ample liquidity in the market, but prices are going up. Those banks that have been reliant on private banking/wholesale funding are bidding up to attract deposits. There has been this kind of skew in the Hong Kong market created by an enormous take up of offshore RMB, but I don't believe that actually there's a systemic problem as yet. And we have a very low A/D ratio of 52% in Hong Kong, so it probably has little impact on us at this moment in time. And we've always had deposits at the center of our funding strategy, as you know.

So I think that what you're actually seeing is probably an increase in margin caused by, effectively, a slight supply/demand imbalance, but that's not across the marketplace. For those banks that have substantial retail deposit bases, this is probably an opportunity for those banks that have been reliant on wholesale funding and their margins are now being squeezed.

John Kirk, Redburn Partners

Okay. So you said this might slow loan growth in Hong Kong or indeed, I don't know how regulators feel about this either, if there's any pressure coming from regulators?

Stuart Gulliver, Group Chief Executive

Regulators are certainly showing some concern at an individual bank-by-bank level, as they rightly should do as potential regulators. But we're not privy to those individual conversations that they're having. The HKMA wrote to all of the bank CEOs reminding them of the need to grow their deposit bases to match their loan growth.

I also think there's some indication as well that some of that high loan growth was due to -- effectively may have been borrowed in Hong Kong, going across the border into China. And given that China is in essence something slowing its economy, some of that pressure has also gone away.

John Kirk, Redburn Partners

Okay. Thank you very much.

Robert Law, Nomura

Could I have three areas please? Firstly, on the expenses, could I ask you whether the second half of the year is likely to be higher than the first as it normally is?

And just to clarify on these restructuring charges you've taken, what's the headcount associated with the restructuring booked in the first half? That's the first area.

Iain Mackay, Group Finance Director

First half versus the second half, Robert, I think you're looking for a forecast again, so I'm probably not going to dish those out to you. I'd probably revert back to some earlier comments that Stuart and I made around building momentum around sustainable saves. But being at the early stages of that, we'll obviously continue the focus in the second half and through to 2012.

When you think about the restructuring charges, $477 million in the first half, $270 million related to software impairments, the balance of $200 million or so, certainly to the extent that those restructurings affect headcount, and we've talked about 5,000 through the half point, then clearly, those restructuring charges cover any headcount effect from that. But if you think about this in the context of the Russian disposition of the Retail Bank Wealth Management that was actually sold to Citibank, the restructuring charges that we took in that regard were absolutely de minimis.

The most significant element of that $200 million actually related to the restructuring of some branches and the regional head office in Mexico in the first half. But certainly, that $200 million addresses the -- included within that is the headcount component of any restructuring in the first half.

Robert Law, Nomura

Thank you. Secondly, in terms of the roughly 10% reduction of headcount that you're looking at on a gross basis, and that equivalent reduction of expenses, or certainly, again, on a gross basis, what kind of revenue impact do you think you would have with that?

Iain Mackay, Group Finance Director

I think, Robert, to the extent -- the $2.5 billion to $3.5 billion remember is very much focused on sustainable saves within retained operations. So to the extent that we looked at removing ourselves from certain Retail Bank Wealth Management businesses around the world, as Paul and the team refocused that business model, then there would be to the extent if we disposed any of those businesses or closed them, there would be a revenue impact.

But I think if you reflect back on some of the pages that we shared with you at strategy day, the PBT coming from those businesses within Retail Bank that we would focus on is absolutely de minimis. So at this stage, until we get into a little bit more of the execution beyond that, which we've already announced, it's probably not appropriate to sit and talk about revenue impact.

Robert Law, Nomura

And then the final area was a broader area as we approach the ICB publication. Can I ask what thoughts you have from overseas regulators as to what approach they might take post ring fencing, if it comes in, in the UK, or what thoughts you may have as to what that implication has for businesses outside the UK for you?

Douglas Flint, Group Chairman

Thanks, Robert. We're not aware of anybody who's thinking of following the UK on a ring fencing approach. It's pretty clear talking to the major universal banking centers, Germany, France, the United States, China, that they continue to see the universal banking model as core to their banking systems.

I suspect there will be interest and observation at whatever proposals are put out, just to analyze them to see whether there is something other people have missed. But the feedback that we're getting from others is that this is not a route that they are contemplating, because they believe the aggregate impact of everything that's been done so far is fairly comprehensive. But of course, it's all hypothetical because we don't know what the ICB will recommend.

Robert Law, Nomura

I'm going to have a follow-up to that. What I was really driving at is whether regulators may potentially take a different approach to your businesses, because there's a reduced effective support from the UK Government as they ring fence only a proportion of the activities?

Douglas Flint, Group Chairman

I don't think so. I think the rating agencies used to give a small amount of credit to a group structure in looking at the ratings of subsidiaries. They stopped doing that explicitly quite a time ago and basically, everyone stands in their own. And I think that is the framework that regulators around the world now very much adopt to; they want to see the capital support in their local country. If there is a parent that's okay, but I don't think that they take an enormous amount of additional comfort from that any more.

Robert Law, Nomura

Thank you.

Simon Samuels, Barclays

Just a quick question, really, on the fact that your total balance sheet grew by about 10% in the first half of the year, and your risk-weighted assets only by 5% or 6%. And it looks like the big area of difference was North America, and I think there was an earlier question where you commented about a higher proportion of mortgages, where the average risk weighting has come down a lot. So my question really is, is this kind of disconnect going to carry on, do you think? Do you think the RWA growth will now lag the balance sheet growth, going forward?

Iain Mackay, Group Finance Director

Simon, I think as it relates to the runoff portfolios in North America, it's unfortunately the opposite factor that we're experiencing that, as we run down the portfolio, we're not at this stage seeing the same reduction in the risk-weighted assets as there's some adjustment to loss given default and probability of default as we update for some of the economic factors coming through the models.

I think that will turn over the course of the next few quarters, but there's a little bit of a disconnect at that level. But I think what you do see more broadly across the portfolios is a factor that Stuart mentioned as it relates to net interest margins. A re-mixing away from some of the unsecured products into secured lending across a number of the regions. And certainly, overall, the quality of the assets that we're putting in the balance sheet, whether it's in Hong Kong, other areas within Asia, Latin America, has been maintained, and continues to have a very tight focus around the quality of new business that we're writing. Whether it's the loan to values on UK mortgages, Hong Kong mortgages, again they're underwritten at very low LTVs.

So I think overall, the focus obviously is putting high quality assets in the book and focusing very strongly on the impact that that has on risk-weighted assets and consequent effect on returns.

Simon Samuels, Barclays

Thanks.

Stuart Gulliver, Group Chief Executive

Okay, thank you all very much. Thanks very much for joining the call. We look at this first half as a first small step in the right direction on a very long journey to execute the strategy we set out on May 11, clearly with much more to come. Thank you for your interest in HSBC.

Forward-looking statements

This presentation and subsequent discussion may contain certain forward-looking statements with respect to the financial condition, results of operations and business of the Group. These forward-looking statements represent the Group’s expectations or beliefs concerning future events and involve known and unknown risks and uncertainty that could cause actual results, performance or events to differ materially from those expressed or implied in such statements. Additional detailed information concerning important factors that could cause actual results to differ materially is available in our Interim Report. Past performance cannot be relied on as a guide to future performance.