Edited Transcript

Annual Results 2013

Presentation to Investors and Analysts

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Corporate participants
Stuart Gulliver, Group Chief Executive
Iain Mackay, Group Finance Director
Douglas Flint, Group Chairman

HSBC

Douglas Flint, Group Chairman

Good morning from London, good evening to everyone in Hong Kong, and welcome to our 2013 HSBC annual results conference all. As has been said, I'm Douglas Flint, the Group Chairman. With me are Stuart Gulliver, the Group Chief Executive, and Iain Mackay, the Group Finance Director.

Before we start, I'd like to say a word on behalf of the Board. We consider HSBC to have delivered a sound financial performance in 2013, with good momentum in areas of targeted investment. The Group's capital position strengthened further during 2013.

The core Tier 1 ratio improved to 13.6%, compared with 12.3% at the start of the year. Our estimated CRD IV endpoint basis common equity Tier 1 ratio also improved to 10.9%.

The first implementation phase of the strategy that Stuart set out in May 2011 has now come to an end. The results that we have announced today flow, in large part, from the repositioning of the Group and from enhanced risk controls given effect over the last three years.

This progress, together with a strong capital position, has allowed the Board to increase the dividends per ordinary share in respect of the year by 9%.

Stuart will now talk you through the highlights for the year; Iain will take a detailed look at the financial performance; and finally, Stuart will cover the next phase of the strategy. Stuart.

Stuart Gulliver, Group Chief Executive

Thanks, Douglas. I'll start by pulling out the key points. As Douglas said, our performance in 2013 was influenced by the strategic measures that we have taken since the start of 2011.

Reported profit before tax was $22.6 billion in 2013, up 9% on 2012. Underlying profit before tax was $21.6 billion, an increase of 41%. And the reported return on average ordinary shareholders' equity was 9.2%, up from 8.4% in 2012.

As Douglas indicated, we remain of the best capitalized banks in the world, with a core Tier 1 ratio of 13.6% and an estimated CRD IV endpoint basis common equity Tier 1 ratio of 10.9%. We therefore remain well placed to meet expected future capital requirements, notwithstanding a continually evolving regulatory environment.

The advances to deposit ratio remains robust at 72.9%. And we also continued to demonstrate our ability to generate capital, which allows us to increase dividends for the year by 9% to $0.49 per share, in line with our progressive dividend policy. This cements our status as one of the highest dividend payers in the FTSE, and we'll talk later about the strategic highlights of the last three years, as well as priorities for the three years ahead.

Turning now to slide 4, this slide lays out the financial highlights, as I've just discussed. The additional point to note here is the cost efficiency ratio, which improved to 59.6%. And, as we explained in May at our investor update, we've modified the cost efficiency target for the next three years to mid 50%s to more appropriately reflect the composition of the Group's profit. Earnings per share also increased from $0.74 in 2012 to $0.84 in 2013.

Turning to regional and business contributions, underlying profits were higher than 2012 in five out of the six regions. In Hong Kong, underlying profit before tax was $8.1 billion in 2013, up 13% on last year. This was driven primarily by retail banking and wealth management in global banking and markets. Higher revenue partly reflected average balance sheet growth, increased net fees from unit trusts and debt issuance, and increased collaboration between commercial banking and global banking and markets.

In the rest of Asia-Pacific, profit was $6.7 billion, up 20% on 2012, though it was broadly unchanged excluding the net impact of the Ping An disposal. In accordance with our strategy, we took action to strengthen our position in most of our priority markets, and also to reduce fragmentation across the region.

In Latin America, profit was $0.7 billion, down 62%, driven primarily by a rise in loan impairment charges. Whilst our performance in Latin America was affected by slower economic growth and inflationary pressures, we made significant progress in repositioning our portfolios, with a focus on our priority markets of Brazil, Mexico and Argentina.

In Europe, profit was up $2 billion, due to significantly lower customer redress provisions, higher revenue in commercial banking, a resilient performance in global banking and markets, and higher mortgage lending in the UK.

North America returned to profit at $1.6 billion, due mainly to a decline in loan impairment charges in the US and lower costs, due to the non-recurrence of provisions for fines and penalties recorded in 2012. The reduction in loan impairment charges was primarily in the run-off portfolio, partly reflecting improvements in the housing market.

Next, I'll run the results broken down by the four global businesses. In commercial banking, we achieved profit of $7.9 billion, up 5% on 2012. Revenue growth was driven mainly by Europe and Hong Kong, partly offset by Latin America and North America.

We also recorded loan growth of more than $13 billion, driven primarily by term and trade-related lending and, to a lesser extent, commercial real estate and other property-related lending. Trade-related revenue was affected by spread compression, although this began to stabilize in the latter part of the year.

In global banking and markets, profit was $9 billion, up 15% on 2012, driven by higher revenue and significantly lower loan impairment charges and other credit risk provisions. The increase in revenues was, in part, underpinned by a resilient performance in the majority of our customer-facing businesses, particularly in credit, equities and capital financing.

We believe this result demonstrates, again, the strength of our differentiated business model with its broad international focus, emphasis on customer connectivity, product capability and our balance sheet strength.

In retail banking and wealth management, profit was up $2.4 billion as we made further progress in running off the consumer mortgage and lending portfolio in North America, with an improvement in loan impairment charges more than offsetting the decline in revenue.

Our retail banking and wealth management business, excluding the US run-off portfolio, what we call our principal retail banking and wealth management business, benefited from lower UK customer redress charges and further sustainable cost savings, together with revenue growth, mainly in Hong Kong and Europe. This excludes the loss on the sale of the HFC Bank's secured lending portfolio.

In the UK, we loaned GBP3.8 billion, or $6 billion, to help more than 30,000 first-time buyers purchase their own home in 2013. We also provided greater convenience for our customers by rolling out our new mobile applications across 25 key markets with 2.5 million downloads over the course of the year.

Finally, we remain committed to global private banking and to repositioning the business. This repositioning, together with legacy issues, resulted in a reduction in profit of $0.7 billion in 2013. But our teams remain focus on the collaboration between global private banking and commercial banking, which is where we expect the majority of our new clients to come from.

Before I hand over to Iain, I'd like to make a few key points. First, on revenue, by growing our organic business since the start of 2011, we have already replaced approximately one-third of the reduction in total revenue from the 63 disposals or closures that we have initiated.

Second, we've introduced new incentive plans for retail banking and wealth management globally, which removed the formulaic link between product sales and variable pay. We therefore expect future revenues to be of a higher quality with lower risk of customer redress.

And, third, on a constant currency basis and excluding UK customer redress and restructuring costs, operating expenses were broadly flat in 2013, compared to 2010. This demonstrates the impact of our sustainable cost savings and disposals in broadly offsetting cost increases over the period.

These included inflationary pressures, the UK bank levy and investment in risk and compliance, as well as other business initiatives. This is a clear demonstration that we're absolutely able to manage the firm, on a global basis, to drive revenue growth and manage costs.

I'll now hand over to Iain to talk through the financial performance in more detail.

Iain Mackay, Group Finance Director

Thanks, Stuart. This slide shows the reported results. Let me highlight a few key points.

Reported revenues were down, compared to 2012. This was driven principally by lower net gains from disposals and reclassifications, mainly as 2012 included gains from the disposal of the US cards and retail services business of $3.1 billion, and the disposal of our investment in Ping An of $3 billion.

Operating expenses were down $4.4 billion, mainly reflecting the non-recurrence of the provision for US anti-money laundering, the Bank Secrecy Act and Office of Foreign Asset Control investigations, lower charges relating to UK redress programs and lower restructuring and related costs. Loan impairment charges improved significantly, particularly in the US where we continue to run off our consumer mortgage and lending portfolio.

As you'd expect, the contribution from associates fell as a result of the sale of our shareholding in Ping An last year and the reclassification of Industrial Bank as a financial investment.

Turning to slide 7, let's look briefly at the discrete fourth quarter where reported profit before tax decreased by 11%, compared to the fourth quarter of 2012. Excluding movements in the fair value of own debt, and the impact of any gains or losses on disposals, as well as the operating results, revenue increased.

This was driven by global banking and markets and commercial banking, but was partially offset by lower revenue in retail banking and wealth management and global private banking.

Loan impairment charges improved significantly, particularly in commercial banking in Europe and in the US run-off portfolio. Whilst operating costs were lower, as a result of the non-recurrence of fines and penalties, lower customer redress, and decreased restructuring and related costs, these were partly offset by the increased UK bank levy.

More detail now on the underlying numbers, as it is on this basis that we measure our performance. As a reminder, our underlying numbers eliminate changes in the fair value of our long-term debt due to own credit spread, removal any gains or losses on disposals as well as the operating results of those businesses in both 2012 and 2013, and eliminate foreign currency translation differences. They do not exclude anything else.

Underlying revenue was up $1.7 billion, or 3%, compared with 2012. Loan impairment charges were down $1.9 billion, or 25%, and operating expenses were down $2.6 billion, or 6%. This performance, higher revenues, lower loan impairment charges and lower costs, meant that underlying profit before tax was $21.6 billion, up $6.3 billion, or 41%, compared with 2012.

Turning to slide 9 to look at revenues. Underlying revenue was $63.3 billion, up $1.7 billion on 2012. We've brought out some of the selected items which includes revenue, many of which we've discussed earlier in the year.

These include a net favorable movement on non-qualifying hedges of $807 million, a net gain recognized on completion of the sale of our remaining investment in Ping An of $553 million, which offset the adverse fair value movement in 2012, and a number of other smaller items which we've previously covered.

Taking you through the global businesses in turn, from left to right on this slide, in global banking and markets revenue was $915 million higher than 2012, which, in part, reflected a resilient performance across the majority of our customer-facing businesses and reflects the strength of the business model.

Revenue increased notably in credit, equities and capital financing. As expected, balance sheet management revenue decreased as proceeds from the sale and maturity of investments were reinvested at prevailing rates which were lower, together with reduced gains on the disposal of available for sale debt securities.

Additionally, in 2012, revenue included a reported net charge of $385 million as a result of a change in estimation methodology and respect of our credit valuation adjustment of $903 million, and a debit valuation adjustment of $518 million to reflect evolving market practices.

In commercial banking, revenue was $312 million higher than in 2012. This was driven, in part, by average balance sheet, partly offset by spread compression, together with higher lending fees and improved collaboration with other global businesses.

In our principal retail banking and wealth management business, which you will recall excludes the US run-off portfolio, revenue was marginally higher by around $100 million. This increase reflected improved mortgage spreads and mortgage balance growth, notably in our home markets of Hong Kong and the UK.

There was also higher fee income in Hong Kong, mainly from unit trusts and broking income. These were partly offset by reductions in revenue in the rest of Asia-Pacific and Latin America, in part reflecting adverse movements from the present value of in-force assets and in insurance operations, compared with 2012.

In the US run-off portfolio, revenue was lower by $1.1 billion, reflecting lower average balances, losses on the sale of US legacy non-real estate and real estate loan portfolios, of $271 million and $153 million respectively, and losses in the early termination of cash flow hedges of $199 million.

In private banking, revenue was down $368 million. This partly reflected lower net interest income, as higher yielding provisions matured, and limited opportunities for investment, due to lower prevailing yields, coupled with narrower asset spreads and lower average deposit balances.

In addition, revenue fell as a result of lower client assets and ongoing repositioning of the business. However, we attracted positive net new money of $4.6 billion from our clients in Asia in 2013.

Turning to operating expenses; we continued to exercise strict cost discipline, and achieved $1.5 billion of sustainable cost savings during the year. This takes the annualized total to $4.9 billion since the start of 2011, as we continued to release funds to invest in growth, in line with our strategy.

Overall underlying costs were down $2.6 billion, or 6%. This mainly reflected the non-recurrence of provisions for fines and penalties recorded in 2012, lower charges relating to UK customer redress programs, and lower restructuring and related costs.

Excluding these items, cost are $108 million higher than in 2012, reflecting a number of items. An increase in the UK bank levy charge of $444 million; a provision in respect of regulatory investigation in global private banking; an increase in litigation-related costs, primarily in respect of Madoff litigation in global banking and markets; and a customer remediation provision relating to our former US cards business.

We also increased spending on targeted organic growth and infrastructure, and continued to invest in regulatory requirements, particularly through our global standards program. Other costs rose, due to higher operational expenses, partly driven by general inflationary pressures of around $900 million.

Costs benefited from our sustainable savings, and an accounting gain arising from a change in the basis of delivering ill health benefits to certain employees in the UK Bank of $430 million.

We achieved positive jaws of 9% for the year.

Turning now to credit quality; underlying loan impairment charges were down $1.9 billion, or 25%, compared with 2012. We saw declines in the majority of our regions, particularly in North America, where loan impairment charges fell by $1.9 billion.

This partly reflected improvements in the US housing market; reduced lending balances from the continued portfolio run off, and loan sales; and lower levels of new impaired loans and delinquency in the US CML portfolio. These factors were partly offset by an increase in Latin America.

In Mexico, we saw specific impairments in commercial banking relating to homebuilders, due to a change in public housing policy, and higher collective impairments in retail banking and wealth management.

In Brazil, loan impairment charges increased, due to changes to the impairment model, and assumption revisions for restructured loan account portfolios in retail banking and wealth management, and business banking and CMB, as well as specific impairments in commercial banking. However, following policy changes made in previous periods, the credit quality in the remainder of the book in Brazil has improved.

Turning now to the drivers of returns, on slide 12. The strengthening of our return on equity from 8.4% to 9.2% was due, primarily, to favorable impact from lower adverse movements in the fair value of our own debt; a reduction in notable cost items, primarily from provisions for fines and penalties in customer redress; and the net gain recognized on the sale of our investment in Ping An, which offset the adverse fair value movement in 2012. However, these were partly offset by lower net gains on disposals, and the exclusion of their operating results.

Our current return on risk-weighted assets stands at 2%, on both a reported and an underlying basis. Excluding the run-off portfolios, it is 2.2%, including 20 basis points of notable items. We have provided a breakdown of the Group underlying return on risk-weighted assets by global business, and split out the legacy portfolios for global banking and markets, and retail banking and wealth management.

Looking forward, our return on equity will mainly be influenced by our success in executing components of our strategy, and our ability to navigate ongoing regulatory uncertainty.

There is also a technical accounting matter relating to BoCom. BoCom is accounted for under the IFRS equity accounting method. This means that, when the investment carrying amount of BoCom in our books is more than the calculated accounting value in use, any further recognition of the share of its profits will be reversed.

While this is likely to affect our earnings at some point in 2014, it has no impact on our cash flow, no impact on our progressive dividend policy or regulatory capital, and no impact on our long-term strategy towards BoCom.

Turning to slide 13; the after-tax distribution of profits in 2013 is similar to that of 2012. We've retained 53%, and increased our distribution to shareholders to 35%. This is reflected in the 9% increase in the dividends for 2013. 12% was allocated to variable compensation.

As you can see, we've increased the fourth interim dividend to $0.19 per share, in line with our progressive dividend policy. And we currently plan to deliver the first three interim dividends of $0.10 per share in 2014.

Turning now to capital. The Group's core Tier 1 ratio was 13.6% on December 31, 2013, compared with 12.3% in the prior year. This reflects strong net capital generation of $10.1 billion, in addition to the $7 billion that we paid in dividends net of scrip during the year.

One of the key contributors was the continuing management of our run-off portfolios, which released $40.8 billion of risk-weighted assets in 2013. From the beginning of 2011 to the end of 2013, we've reduced risk-weighted assets by approximately $90 billion, as a result of disposals and closures, with potentially $5 yet to come.

Our estimated CRD IV endpoint basis common equity Tier 1 ratio was 10.9% at the end of 2013. This figure includes five dividend payments in respect of 2013, with the fourth quarter interim dividend now deducted from capital. This is a one-time adjustment, in line with CRD IV requirements. We're well positioned with respect to the implementation of CRD IV.

Uncertainty remains around the amount of capital that banks will be required to hold, as key technical standards and consultation from regulatory authorities remain pending. We await clarification from the PRA on the quantification and interaction of CRD IV capital buffers, and Pillar 2, and also, a number of EBA technical standards, and CRD IV implementation, which will be delivered in 2014.

In addition, the PRA has given notice that it will implement loss given default floors across selected portfolios during the first quarter. This will increase our risk-weighted assets in the first quarter of 2014, with an estimated reduction in our common equity Tier 1 ratio of 25 to 35 basis points.

HSBC remains one of the best capitalized banks in the world, providing capacity for both organic growth and dividend return to shareholders.

I'll now hand back to Stuart.

Stuart Gulliver, Group Chief Executive

Thanks, Iain. So 2013 marked the final year of the first implementation period of the strategy that I outlined back in May of 2011. You'll recall that our strategy aims to capitalize on two major trends; the continuing growth of international trade and capital flows; and wealth creation, particularly in Asia, the Middle East and Latin America.

Over the last three years, we've put this strategy into action, pursuing more effective capital deployment, greater organizational efficiency, and better returns. And it is worth restating that we've already replaced approximately one-third of the reduction in total revenue that came about from disposals.

As I explained earlier, we have a firm grip on costs, and have demonstrated our ability to grow the business. The Group today is leaner than in 2011, with strong potential for growth.

2014 marks the beginning of the next phase of the implementation of our strategy, and there are three priorities for the next phase, as we announced at the investor update last May. It's important to stress that these three priorities are absolutely equal, and we will pursue each of them with equal intensity.

First, we aim to grow the business and dividend. So we're going to continue to invest in organic growth opportunities that are aligned to our strategy, consistent with our risk appetite, and which add value to the Group. In particular, we'll increase collaboration between our businesses, further improve connectivity between regions, and build on our core strengths.

In doing so, we're going to aim to capitalize on our global footprint, particularly in our leading business areas such as trade finance, payments and cash management, and foreign exchange. We will also continue to invest in high growth markets, such as the Pearl River Delta, and ASEAN, and improve our position in highly connected developed markets, such as Germany and the United States.

Our capital strategy aims to increase dividends progressively. And if we're unable to deploy remaining capital ourselves, in such a way that it provides incremental value for our shareholders, we may seek to neutralize the effect of the scrip dividend through share buybacks, subject to regulatory approvals. And we shall, of course, continue to wind down and reduce the impact of the portfolio of legacy businesses.

Second, we'll continue to implement our global standards program, which we believe will increase the quality of the Group's earnings. Global standards concerns all of our activity and will drive consistently high standards throughout HSBC.

We have made substantial investment in risk and compliance capabilities across all businesses and regions, to strengthen our response to the ongoing threat of financial crime, and will continue to do so. This is the right thing to do, in line with our values, and we believe that it will also become a source of competitive advantage.

Third, we aim to deliver a further $2 billion to $3 billion of sustainable savings by streamlining our processes and procedures without, in any way, compromising our commitment to compliance and global standards. We'll achieve this by taking advantage of the considerable scope within the business to globalize and simplify many of our operations and practices.

And finally, a quick word on outlook. We remain of the view that China will grow its GDP by about 7.4% this year, the UK by 2.6%, the USA by 2.5%, and Western Europe by 1.2%. And although there's been a sharp selloff in some emerging markets, both when tapering was first talked of last June, and more recently, in January this year, we see this as a reflection of specific circumstances rather than a generalized retreat.

The countries most affected have two common themes; namely, large current account deficits, and the uncertain outcomes arising from elections within this year. By contrast, other emerging markets, such as Mexico, have been upgraded by the rating agencies in exactly the same period.

Overall, we remain optimistic about the longer-term prospects of the emerging markets, and especially the opportunities for HSBC, which will arise from the anticipated material expansion in south-south trade and capital flows.

In the short term, we stress the importance of differentiating within, and between, individual countries within the generic category of emerging markets. Nevertheless, we anticipate greater volatility in 2014 and choppy markets, as adjustments are made to changing economic circumstances and sentiment.

Now I'm going to take your questions. The operator will be happy to explain the procedure and introduce the first question.

Questions and Answers

Chirantan Barua, Sanford Bernstein

I have three quick questions. The first one is on the PRA floors. It almost sounds like countercyclical capital already kicking in. It would be great if you could give us some idea on which floors, regions, businesses that these floors will impact.

The second one, Stuart, is on Hong Kong outlook. You've given your guidance on greater volatility and how some emerging markets impacted, others are not. Not too many transactions happening in Hong Kong at the moment in the property space; it would be great to get 2014 outlook.

The last one is on BSM, if you have any updated guidance on BSM and how you're going to deploy the huge amount of cash which is on your balance sheet.

Stuart Gulliver: Sure. Let me take BSM -- we'll do them in reverse order, so BSM I think guidance is $2.5 billion for 2014. Curves again have flattened out; you had a little bit of steepness and then they flattened back again. We're going to clearly keep the book short. We're not sure at what point short-term rates start to back up. We don't want to be caught with assets that actually we're then having to fund at higher running rates.

So $2.5 billion is guidance for 2014. We're still at this inflection point. We saw, effectively, a sell-off in the long end, so the curve's steepening from the long end. We haven't seen any movement at the short end but that, clearly, is something we've got to navigate quite carefully.

Hong Kong, I think the property market in Hong Kong will remain soft during 2014. The government restrictions were there to take the heat out of the property market; they haven't really changed. Volumes, as you say, remain reasonably low in the property market. I don't see that particularly changing during the course of 2014.

I think it will be a soft property market, but remember, LTVs on the book in Hong Kong overall are sub-40% and, therefore, I'm not concerned from a credit quality point of view and a bad debt point of view. Actually, the volume of activity in terms of mortgages has dropped a little bit, but we haven't seen a significant impact in terms of the P&L of the retail banking and wealth management business.

Actually from an equity/capital markets point of view, there's actually quite a significant M&A pipeline, a corporate finance pipeline, actually in Hong Kong for this year. So I think that we may, ironically, see an offset from any softness in the mortgage part of retail banking in Hong Kong coming through in terms of the corporate finance IPO-type of pipeline, which actually will support the wealth part of retail banking and wealth management.

So Hong Kong outlook, yes, property market is soft but overall, I still think that we will be able to see growth in PBT in our operation in Hong Kong.

I'll hand over to Iain on the PRA floors.

Iain Mackay: As you'll recall, we certainly saw a couple of PRA floors introduced in 2013, probably the most notable of which was on sovereigns outside the European economic area. What we refer to, with respect to the first quarter, is largely with respect to corporate portfolios, and mostly within the developed economies of the UK, Europe, and the US, which again, the PRA has indicated their intent to implement a loss given default floor of 45%.

That's driven particularly by the concern around the level of data that the PRA would like to see in terms of how we support and develop the internal ratings-based models. So clearly, from our standpoint in mitigating some of this impact, we continue to drive down on the granularity of that data but this, again, is principally focused on corporate portfolios in the developed markets.

Chirantan Barua: Thank you.

Chintan Joshi, Nomura

You've already discussed a little bit in the opening remarks, but my first question is on asset quality. What kind of impact are you seeing from the January FX volatility we've seen, and if you could specify the areas of concern for you? And I've got two more.

Stuart Gulliver: Okay. We haven't seen any particular credit issues arising out of the FX volatility that's taken place in Brazil, India, Indonesia, or Argentina.

Chintan Joshi: You broke off towards the end.

Stuart Gulliver: There has been no impact on the credit quality of our loan book from FX volatility so far this year in Brazil, India, Indonesia, or Argentina.

Chintan Joshi: What are your expectations, going forward?

Stuart Gulliver: Our expectations are that, depending on how that volatility continues throughout the year, we may see some impact in terms of bad debts, most likely actually through CMB and SMEs, but it really depends on what happens in the balance of the year.

We have been very conservative in terms of our exposure to global banking and markets' clients and, therefore, have made absolutely sure that they clearly have borrowed. If they've borrowed foreign currency, they have foreign currency revenues.

What you may find is that actually, as GDP slows, some of the smaller customers are impacted by the GDP slowing, not directly by the FX, but by the second order impact. That tends to be what happens when you have these kind of sharp currency moves, unless they're corrected reasonably quickly. But again, we have no line of sight to that, at the moment, to be adjusting any kind of loan impairment charges.

Chintan Joshi: Thanks. My second question is on trade finance. You do report in a couple of different areas. Holistically, how do you see trade finance margins having developed in Q4?

Also, if you could give us some indication of what current level of profitability is in that business in terms of ROE?

Stuart Gulliver: Okay, so our volume of lending in trade finance increased by about 20% over 2012, driven mainly by Hong Kong, rest of Asia-Pacific. The margins in 2013 were quite a bit lower, but actually we've started to see that decline in margin bottom out, so this is a subtle point

I'm going to make. The rate of margin compression has slowed into the third and fourth quarter. It hasn't stopped and gone back in the other direction, but the rate at which margins were being squeezed has slowed down.

This remains, actually, a very profitable business for us, with a substantial ROE. I don't know, Iain, if we have a RWA on it.

Iain Mackay: We don't disclose that separately.

Stuart Gulliver: We don't disclose it separately, but it's a great business. Really, if you think about what we've done is the revenue is broadly unchanged versus 2012 because we pumped volumes up by 20%, which offset the margin decline.

Iain Mackay: Broadly, if you think about returns in this one, Chintan, the targeted returns and return on risk-weighted assets for the commercial bank ranges from 2.2% up to 2.5%. Given the capital intensity of this business, the returns within the global trade receivables financing business is quite strong in that range.

Chintan Joshi: Thanks. My final is, there are a lot of notable items, but even outside the notable items, there's a lot of non-recurring impact to revenues and cost. I just wanted to ask you how do you see current underlying, adjusted, if you may, revenue growth, cost growth year on year, and also what your expectations are for the coming year. Thank you.

Iain Mackay: That's a new question from you, Chintan. Thank you. Interestingly enough, I would actually say there are many, many fewer notable items in these numbers than has been the case in 2012 or 2011, largely as we've moved through to the latter stages of the reshaping of the business under the strategy.

We provided the key elements that sit within the underlying numbers. Again, the underlying numbers are only excluding three issues; fair value own debt, the currency effect, and the impact of acquisitions and dispositions. Those are the reconciling items.

But broadly, within that, we're slowly, I hope, working towards the end of what we see from a PPI perspective. Stuart made some remarks around how we've repositioned some of the incentives within the retail banking and wealth management business to improve the quality of our earnings in that respect, going forward.

I think, from a litigation standpoint, there's very detailed disclosure on this in note 43 to financials, as well as in the provisions notes in note 31. So again, I think litigation and the risk of litigation is an ongoing feature of any banking business at this point. We've never really broken that out as notable items in the past, but we give you some fairly detailed disclosures as to that which we've incurred this year.

If you look at the revenue line, we've taken some losses as we've run down the CML portfolio in the US, and I gave you some details of that in the revenue walk. And really, from a cost perspective, it's about litigation and it's about customer redress where, again, we've given you some of the detail of that in financials. But going beyond that, I would say we've got a set of numbers here that are beginning to migrate to something that looks more like the normal.

Stuart Gulliver: And if you look under it, revenue growth is about 3%. As I say, bear in mind we've sold 63 businesses that most analysts seem to have kind of not focused on. We've sold an awful lot of revenue, so when you actually look at the revenue numbers and say, well, there's no revenue growth here, people aren't really taking account of the fact that we actually sold substantial amounts of revenue as we sold businesses that were not strategically logical, portfolios of assets that failed the six filters and, obviously, have released risk-weighted assets through that which we've been able to redeploy in growing revenues which are logical within our GBM, RBWM, CMB private banking businesses, which actually, logically, should have a higher valuation.

Chintan Joshi: So would you venture some expectations we should set for the next year?

Iain Mackay: No, not really. Think about the aims that Stuart provides here and the outlook around GDP development, and we've talked about this on numerous occasions in the past, it tends to be a reasonable indicator of our opportunity for growth within those markets.

Chintan Joshi: Fair enough. Thank you.

Alastair Ryan, BofA Merrill Lynch

Three, if I may? First, back to our old favorite regulation and its never-ending development. So since last May you've probably $50 billion or $60 billion more of risk-weighted assets with these new floors that are coming in than you'd reasonably expected to have, and you're running a higher reported common equity Tier 1 than your goal, significantly in excess of 10% versus a goal of in excess of 10% and likely to be building further as you run off legacy portfolios and retain profits. So can you work us back to whether the 12% to 15% target that you reiterated last May is still a reasonable one? Just because the rules keep changing at quite a rapid pace.

Second thing; the restatement of repos makes the margin very difficult to read, period over period. From your commentary it sounds like the margin has stabilized, the Group net interest margin; can you just walk us through that please?

And third on BoCom; I've found it on page 510, which probably is a new record even for HSBC. Are you basically telling us that, unless the share price goes up, you'll have to reverse out the profits that you'll accrue this year, or is it a non-intuitive accounting piece? Thank you.

Stuart Gulliver: Let me kick off on the regulatory capital point and then we'll walk through the repos.

You're right in what you're setting out as a sort of question and, actually, it's not one that we can easily answer, because until we have specific clarity, and this comes from the PRA, about what our end state Tier 1 capital ratio is, we have no choice but to continue to build our capital up and there's several points under that.

One, we clearly are building capital up. If you look at $10.1 billion added to our Tier 1 capital ratio, $9.2 billion paid in dividend, so clearly, we don't have a problem building up to a higher number. But then you get to the second point, which is, well, can you get the 12% to 15% ROE if the E is now substantially higher than your assumption? And the obvious answer to that will be, no, we won't be able to, depending on what actually that eventual E is. What I think I'm confident of saying, Alastair, is that, no matter what the E is, we'll generate a return above our cost of equity.

Whether the 15% becomes impossible to do, and it becomes 12%, or something similar, we just don't know, because, absolutely, there are two things going on here. RWA density, for want of a better expression, keeps changing, floors keep being introduced, and there are some more floors coming in the first quarter on corporate books, which Iain can talk about. And we actually don't know what the end number is. So until we get specificity around all of that and we know what the E is, then only at that point can we revisit the ROE targets.

But again, what we do have the ability, at HSBC, to do, is we don't need to raise equity, or raise capital, to get to these new whatever the Tier 1 ratio they require us to have is because, clearly, we are generating substantial amounts of retained earnings, and substantial amounts of PBT. But you're right; I don't know, at this point in time, whether the 12% to 15% is a reasonable number because I don't know what the E is going to be.

Iain Mackay: And, Alastair, if you think about the operational measures at the business level that we use here, its return on risk-weighted assets, in the year we generated a return on risk-weighted asset of 2%, which is up on last year, and you take out the effect of the legacy assets and global banking and markets and the run-off portfolios in the US consumer business, you're at 2.2%, which is very much in the range that we've set for the Group that triangulates the lower end of the 12% to 15% range.

On an operational level, you can see your way to the lower end, but that excludes, obviously, consideration of how equity develops. And that's the big uncertainty, as Stuart laid out.

In terms of looking at NIMs, with or without the impact of repos within the numbers, we saw net interest margin stabilizing in the second half of the year, particularly towards the end of the year. The rate of decline, as Stuart mentioned, has reduced significantly. This is all good news, but I would call it stability as opposed to recovery. So if you look at where NIM is at the end of 2013 versus 2012, we still have not recovered where we were at the end of 2012, and have some way to go in that regard.

Looking at BoCom, again you've got the prosaic elements of equity accounting under international accounting standards here. Where we've got a market value in BoCom, which has traded well below book value of BoCom in our carrying value now for the better part of two years, and as a consequence of which, and we do this for all our positions on a very regular basis, is reevaluate the accounting against the equity method using a value-in-use model.

What we're really saying to you here is that we believe there's some point during 2014 where the carrying value is likely to exceed our value in use. At that point, we would reverse out our share of the revenues and the profits of BoCom. That's what it boils down to. It in no way has an adverse affect on cash or capital, but certainly it has an impact on reported profits, probably for the second half of this year.

Alastair Ryan: Thank you. Just last stupid part of that question then, can you -- you'll stop accruing BoCom's profits, or you'll take a hit on the book value of it?

Iain Mackay: What you'll do is you'll actually continue to accrue the profits, and you'll take a reverse out of those profits to the extent that the carrying value exceeds the value in use. Now bear in mind this is driven largely by market values. So to the extent that market value is recovered, then our assessment of impairment would change. So this is not an irreversible change; this is just a reflection, on an ongoing basis, of our carrying value versus that of the value in use.

Alastair Ryan: Okay. Thank you.

Raul Sinha, JPMorgan

Can I just follow up on the last one, and then I've got two separate ones? Just on the BoCom accounting impact, I do get the fact that it obviously has no impact on cash flow, or capital. But is there a broader point to think about your dividend payout ratio, while excluding the share of contribution from BoCom, going forward, just given that this volatility that causes to your earnings stream? Do you think that would be a reasonable way to look at your dividend payout ratio, going forward?

Iain Mackay: No I wouldn't. I don't see BoCom having any adverse effect on dividend paying capability at all. The actual cash realized from BoCom in the form of dividends to us is a very, very, small amount for the Group on an ongoing basis. It's actually one of the features that drives the carrying value; obviously, dividends would be a deduction from carrying value. So it's one of the things that continues to drive up carrying value against our value in use. So no, I would not reflect on this as having an adverse impact in the dividend paying capability of the Group at all.

Raul Sinha: Thanks. And then just two other questions. Just wanted to ask if you could share with us your estimate, or your thoughts, on what your Pillar 2A buffer might be. Some of the other UK banks have obviously given that number to us recently, so I was wondering if you might be able to do that as well.

Iain Mackay: Not inclined to provide that, Raul. That really is actually confidential between the PRA and the Bank, and I believe that one or two of our competitors appealed to the PRA for special permission to release that to you. We have a strong capital position. As Stuart mentioned, we generate capital to a very significant degree on a quarter-by-quarter basis, supporting strong dividend payments to the shareholder base.

Our capital position, common equity Tier 1 at 10.9%, is certainly above our current understanding of what the PRA would require of us, substantially above that. But what we are not clear on, and this was the point that Stuart was making, is we don't know where the endpoint in this is. So as the EBA finalizes ITS and RTS on the implementation of CRD IV, and the PRA then interpret that for application in the United Kingdom, the interaction of the various buffers, as we work through the transitional period, and the size of those buffers, is actually what we need to understand.

So we'll continue to work through the consultation processes; the PRA is ready to engage in that. And hopefully, as 2014 rolls on, we'll be able to give greater guidance to the marketplace about where we think that endpoint ultimately is, and going to an earlier question, hopefully inform where we think that has any impact on our ability to generate returns on equity, and wider dividend distribution. It's an area where there's a lack of clarity right now and, at this stage, we don't particularly feel that it would be beneficial to anybody to do some gross speculation as to where it might end up.

Raul Sinha: Okay. And then, I get all the commentary about redeploying your capital into higher return on risk-weighted assets, and obviously that's a very sensible strategy across the Group. I'm just a little bit worried about the fungibility of your capital across subsidiaries. And I was wondering if you could comment on the excess capital that is now in the US and what you might, or might not, be able to do in terms of redeploying that into higher return RWAs.

Iain Mackay: Yes, absolutely, Raul, you follow the way in which we manage capital distribution within the Group. The subsidiaries around the world return their surplus capital to us in the form of dividends. That then supports the dividend to the shareholder of HSBC Holdings plc, as well as supporting the redistribution of some of that capital back into the businesses to support growth in the various geographies, through the legal entities in each of the markets in which we operate.

That practice has not changed. Clearly, our subsidiaries, around the various parts of the world, are having to deal with how their local regulators implement Basel III as well. But, in the round, that approach to capital management will remain absolutely consistent, going forward. When you talk specifically to the United States, as we've mentioned in the past, we believe we've got substantial surplus capital there. But we've also got a couple of businesses on which we're very focused on growing.

Commercial banking is at the forefront of that, supported by global banking and markets. And as we've deployed to the major metropolitan and industrial centers, particularly in the West Coast of the US and in the Midwest, we've seen the opportunity to grow the commercial banking business. The early stages of that is beginning to come through the numbers in the United States, and we'll continue to deploy surplus capital to the development of those businesses, as well as the restructuring of the retail banking and wealth management business.

So there is an opportunity to deploy some of that surplus capital. But as we work through the results of the comprehensive capital analysis and review with the Federal Reserve, hopefully, in the years ahead, we'll find a way to release some of that surplus capital which we believe exists back to the parent, for deployment to other businesses round the world.

Raul Sinha: Is there a specific catalyst, Iain, that you think might be the point at which we can expect a decision to be taken in the US on redeployment of that capital, or a dividend?

Iain Mackay: I think the outcome of the CCAR review by the Fed is important. We'll hear about that towards the end of March. Again, we carry very, very strong total capital ratios in the US; they're just under the 27% mark. Overall, we've got a core Tier 1 ratio of in excess of 13%, nearly 14%, in the US.

So we believe, on a quantitative basis, we'll be in good shape. On a qualitative basis, which by the way is the basis on which a number of our peers in the US have been challenged, in terms of the overall process, the quality, the granularity of the data, like our peers we would expect to be given a list of things the Fed would like to see us improve on.

But I think, beyond CCAR, it is demonstrating the sustainability of profits coming through the US business; it's continuing to make progress in the rundown of the finance company legacy assets, which the team in the finance company's done a great job of, over the course of the last 12 to 18 months.

And then continue to make progress against the various regulatory matters, which we're in the process of investing quite significantly in, the DPA being one; but the continued focus on improving processes as it relates to mortgage lending and foreclosures would be another.

So we've got to make progress on those three fronts, in my view. And until we've made some significant progress on the DPA, I think it's unlikely we'll be given the right to dividend our surplus out to the parent.

Raul Sinha: Thanks very much. Sorry, just to clarify; the DPA's 'til December 2017?

Iain Mackay: Yes, that's right.

Raul Sinha: Okay, thanks. Bye.

Dominic Chan, BNP Paribas

Stuart, it looks like the momentum for less fee income and insurance profit in the fourth quarter slowed down quite substantially in the fourth quarter last year, in particular in Europe and rest of Asia-Pacific. I'm just wondering the reason behind the slowdown in the fourth quarter, and what you think is the momentum going into the current year? Thank you.

Iain Mackay: Dominic, I think certainly, as it relates to fee income, I don't think that's necessarily the case. What we did see in the fourth quarter was some slowing, certainly, in terms of global banking and markets in the rates business, where we saw revenues a little bit slower. I think when you look at overall revenue development, we certainly saw the impact of the continued run-off, and disposition of real estate tranches within the US portfolio.

You see the impact of DVA, but that's considerably less than was the case in the same quarter last year. I think, broadly speaking, fee income has held fairly steady, and we've seen an impact in terms of fourth quarter revenues in the other operating income line, and on the trading income, as I mentioned.

But overall, fee incomes remained reasonably steady. It's a little bit down in private banking, and that's driven principally by the repositioning within the global private bank that we're in the throes of doing. But in the round, fee incomes remained fairly stable.

Dominic Chan: Okay. Thank you.

Rohith Chandra-Rajan, Barclays

Just one fairly general question actually, just in terms of growth opportunities for 2014. You note the volatility in selected emerging markets, and believe your GDP forecast's unchanged. Just wondering what your current perception is of growth opportunities within the return targets for 2014 versus 2013? So how would you compare growth opportunities in the two years? Thanks.

Stuart Gulliver: I think you've got to basically go by geography, and then by business within geography. There's no rising tide that will lift boats. So if you look at where I think there'll be greater growth this year versus last, I think the UK for us.

With UK GDP at 2.6%, one of our two home markets, we have a substantial footprint here, the competitive landscape should enable us to take market share in commercial banking, global banking and markets, and indeed in retail banking. You've seen that in our lending to SMEs; you've seen that in our global banking and markets business; and it’s market share in debt capital markets and foreign exchange, and so on. And you've actually seen it in retail banking, with mortgages and CMB with lending to international SMEs.

If you look round the world, I still think China's going to do 7% to 7.5% GDP growth, which will power the Pearl River Delta and Hong Kong.

The ASEAN countries, particularly Malaysia, Singapore, should have reasonable GDP growth; Indonesia, obviously, when it gets through its election. Mexico, with the Pemex reforms, we think it's probably a 4%/5% GDP growth this year and, therefore, we can see substantial opportunities there.

And then if you look at particular initiatives, for us, we don't think global trade goes into reverse. We know that some of the margin compression, or we see and know that some of the margin compression is actually moving through, i.e., it's kind of bottoming out. The volume growth that we've seen is appropriate to our market share in that regard.

I still think RMB internationalization is a big macro play that will benefit this Bank. I think the fact that the RMB get weakened by 1%, which has become a fascinating headline for some of the media, is actually a jolly good thing. You want a two-way market in a currency, if you're going to internationalize it.

So I think there's some specific dig-ins. Again, look at retail banking. We've changed our commission structures last year, to remove any linkage between commissions and individual products sold. That should improve the quality of those revenues, because it should substantially reduce any customer redress risk further down the track.

In global banking and markets, I think we've again proved that we have a differentiated model, which is something that we've been saying for quite some time. And I think we'll continue, if anything, to take market share in the emerging markets, because if this emerging market volatility shakes out a few more competitors, then we stand ready to take that market share.

And then in private banking, we're part-way through a restructuring of that business. It will remain a core business for us.

Last year, we saw $5 billion of new AuM introduced by the commercial bank to the private bank, which is a proof of the new model. We want most of our private banking clients to basically be the self-employed out of our commercial banking business who eventually trade-sell their business, or IPO it.

So you're not going to have, if you like, the rising tide lifts all boats so there's fantastic growth in X, Y or Z, but we can see specific idiosyncratic opportunities that give us some confidence that we'll see growth in our revenue line this year.

Rohith Chandra-Rajan: Okay. Thanks very much.

Tom Rayner, BNP Paribas

Just two, please. The first one just to clarify; the 25 to 35 basis points you flagged up from the floors, that is incremental to the $33 billion increase in RWAs in 2013, which was partly driven by the 45% floor. Is that correct?

Iain Mackay: Yes, Tom.

Tom Rayner: That is correct. Thanks, okay. Just following from that, that gives you, if I factor that in, a pro forma start point of about 10.5%, 10.6%, fully loaded. We don't know Pillar 2A, but if we had a guess at it we could, I think, make a case that your go to capital ratio's going to be somewhere north of 12%, maybe closer to 13%.

And I'm just wondering if, with that in mind, you can update us on your thinking about the payout? Because I know you focus on the 53% net of scrip as a percentage of earnings before variable pay, but we're up to 57% now, on a traditional dividend payout. Can you just update us with that in mind, that whole capital accretion argument, please? Thank you.

Iain Mackay: So Tom, do you know something that we don't? (laughter)

Tom Rayner: Possibly. (laughter)

Iain Mackay: I'm not going to speculate on where this has ended up, because we just do not know how the capital requirements are going to develop in terms of interaction of buffers, the implementation of buffers, over the course of next two to three years.

I think what is perhaps interesting is that the PRA has taken the view that they will, in effect, take all of the transitional arrangements and move them back to the beginning of 2014. So getting to an endpoint on an PRA basis is actually a little bit easier, to the extent there are any transitional arrangements that actually are disadvantageous to us to the tune of about 10 basis points.

So your starting point of 10.5% to 10.6% probably makes sense, at an endpoint common equity Tier 1 January 1 2014. But where we end up, with the consideration of Pillar 2A, Pillar 2B, the implementation of a PRA buffer, countercyclical buffer, sectoral capital requirements, your guess is as good as mine.

I can't really dig into your question a little but further, because you're guessing.

Tom Rayner: Okay. But it sounds as if the payout is the thing which would flex, if something had to flex.

Iain Mackay: Look, again, Tom, this year we generated, excluding the dividend, we generated $10.1 billion worth of capital. Okay? We've got a distribution in terms of how we've used that, or deployed that, with 53% return retained for the future strength of the Group, 35% back to shareholders, and 12% allocated to variable compensation.

The capital generative ability of the operations around the Group is what is important here. So going back to Stuart's earlier statement, we don't have any particular concerns about the ability to generate capital to fund dividends to the shareholders, going forward. I think the question, and perhaps where this comes to the crux, is around what the endpoint capital or equity requirements are and their ability to generate a 12% to 15% return on equity, not necessarily whether we are able to generate sufficient returns and capital to continue to build dividends.

Tom Rayner: Okay. Thank you very much.

Ronit Ghose, Citigroup

Just a couple of questions to follow up. First of all, on Hong Kong, there was very strong loan growth in the first half of last year for you, and there seems to be a bit of a slowdown in the second half. Just wondered if you could put some more color or commentary around that? And vice versa, deposit growth seems to have picked up in the second half.

My second question is on GBM; if I go line by line, the rates business in Q4 has had a very tough quarter, and I know several of the peers have had a tough quarter as well. I was just wondering if you could put some color around, I'm assuming this is the European rates business. And by contrast, equities looks like, unless I've got my numbers wrong, looks like it's had a very -- for a fourth quarter your equity business has had a very good quarter. Is there anything on that, as well?

And the final question is really on -- maybe on more big picture question on China. You're seeing a tightening in the shadow banking sector in terms of, from a policy perspective, non-bank credit is down mid-teens, about 14%, 15%, in January year in year. Do you see any risk of a spillover from that into either your Mainland operations or into your Hong Kong operations?

Stuart Gulliver: Actually, let me just touch on two of the pieces and then I'll let Iain deal with Hong Kong loan growth, although that's probably the HKMA's cooling measures as they came out in the property market. Global banking and markets' fourth quarter rates is the same as everyone else's fourth quarter rates; it's the European rates business.

The equity stuff is stronger in the fourth quarter because we've built a very substantially successful business in Hong Kong, mostly, in terms of equity. So there was actually quite a lot of activity fourth quarter Hong Kong that explains the equity number. And I'll let Iain go into a bit more detail on GBM and Hong Kong loan growth.

As for shadow banking, it's very, very hard to tell the size and scale of the issue, relative to a country with $4 trillion of reserves and a centrally planned economic platform, as to whether -- and where most of the banks are still state-owned, and indeed the local governments can simply start up a local government bond market, the bonds bought by the insurance companies and pension funds domestically, as to how real a problem this is.

The western media clearly would like to see China have a problem. But actually, we're pretty confident with 7% to 7.5% GDP growth. And right now, if you look at our exposure in China, we have exposure to the Chinese state-owned banks, our exposure to corporates and SOEs is quite modest. Most of our China business is actually the high quality Hong Kong developers that have gone north of the border, and multinationals coming into China.

So we're very aware of this issue, and we're very aware of concerns around it, but I don't, at the moment, in terms of China, think there's a particular concern that we are overly-focused on beyond logical risks management.

Iain Mackay: Okay. In terms of Hong Kong loan growth, I think two or three contributors here. The property lending continued to develop, so both from a residential and from a commercial real estate perspective we continued to grow. I think certainly, as the year progressed, we did begin to see some cooling in the residential market on the back of some of the measures, the further measures, taken by the HKMA to try and cool things off on that front, principally with respect to the introduction of an RWA floor of 15% on new business.

We continued to see reasonably good progression on credits we liked within the commercial real estate space across Hong Kong, and we saw the trade and receivables finance business, the volumes that we saw, and although this is fairly short term in nature and the margins took some compression, we saw some fairly significant step-up in volumes in terms of the trades and receivables financing in that respect.

But overall, that's really what drove lending in Hong Kong over the course of 2013 versus 2012.

If you go through the line by line on a management view of operating income within the global banking and markets business, 2013 over 2012, credit had a strong year. We were about $300 million ahead in it. The rates business was actually pretty much of a same story as it was in 2012, and you'll reflect in 2012 that we took a significant benefit in the first half of 2012 on the back of LTRO and tightening spreads in that business.

But overall, the rates business held up pretty well. We did see a weaker fourth quarter, but generally in line with what we saw in the marketplace overall.

Foreign exchange, very much of a sameness with last year, a performance that's very consistent and, as Stuart said, the equities business continues to perform particularly well. We had a really strong year there, particularly in Asia-Pacific. Capital financing, steady growth versus last year; payments and cash management steady growth. Security services pretty much of a sameness with the previous year. And then, balance sheet management, as we've previously guided, down about $600 million in 2012, very much in line.

So that's a broad view of what you saw happening in global banking and markets year on year.

Ronit Ghose: Great, thank you. Just a very quick follow-up on Hong Kong. If I look at the second half of the year versus the first half growth rates, obviously in RBWM but also I think in CMB you've seen a slowdown in growth. I think you've seen a slowdown in growth versus the broader market, based on HKMA numbers. So I don't know if there's anything Company-specific, above and beyond the slowdown in Hong Kong, in the second half of the year?

Iain Mackay: No, don't think so. Certainly, what you saw in retail banking and wealth management was the slowing effect of HKMA measures; we talked about that.

The market, as a whole, saw much slower rates and volumes in the global trade and receivables financing business, in line with, if you like, economic development that we saw in that area in the second half of the year. But I wouldn't point to anything particularly idiosyncratic at all.

Ronit Ghose: Got it. That's really clear. Thank you.

Fahed Kunwar, Redburn

I had a few questions on margin and the UK regulation. The first question, well, it links to the two but, thinking about your total capital requirement in the UK, obviously CRD IV has said that 1.5% of Additional Tier 1 need to be in issue and you've seen a lot of European peers issuing those. And because of your high or low loan to deposit ratio, issuing those, what kind of impact do you see that having on margin?

And also, having to issue, whatever the number is, 4% to 5% on Tier 2 you to have to issue, do you see the issuance of those impacting margins? And would that mean you'd let your loan to deposit ratio run up? Or other unsecured funding would be left to mature?

Iain Mackay: Okay. So it depends really, again, on the future shape of regulation within the UK and perhaps, more specifically, the ring-fenced bank in the UK. You're absolutely right, there's a requirement around 1.5% of Tier 1 instruments and 2% of Tier 2 instruments. But you'll recall already that we've got Tier 1 and Tier 2 instruments in issue, the eligibility of some of which will dissipate over the coming 10 years, as those amortize out under Basel II transitional requirements.

But when we go to the market, and we have gone to market in 2013 with Basel III compliant Tier 2 instruments and our pricing on that was very, very competitive. Again, we saw pricing at spreads that in no way erodes our margin in this respect. So it will be -- and we're talking about funding today that we can deploy into the market profitability.

The question will become relevant at the point at which we've got to issue into the market a much higher proportion than we currently have issued and which we, therefore, as you quite rightly point out, against the strong deposit base we've got, which would make it much more difficult to deploy profitability.

But the extent to which that would be necessary remains, frankly, impossible to determine at this point until we get better clarity on ring-fenced banking regulation in the UK.

Fahed Kunwar: Thank you. My second question was, from your 10.5% starting point, I appreciate we have no idea what the end number will be but the number is probably upward, it seems like the dividend payout ratio won't be flexed to get to that higher capital level. Would you consider -- how are you thinking about potentially higher capital numbers without knowing them, when you're looking at growing your RWAs?

One of your peers is talking about focusing on lower risk-weighted asset businesses to help grow that capital ratio; by definition, I guess that means lower margin businesses. How do you think about your risk-weighted asset growth in the context of potentially higher core Tier 1 requirements?

Iain Mackay: In a manner, that's entirely consistent with how we've thought about it in the last three years, which is now risk adjusted revenue basis. So we've focused on return on risk-weighted assets, targeted within the ranges that we've talked about the investor updates and that we disclose in the financials.

So we have progressively, over the course of the last two years, moved within line with our risk appetite to a lower risk position. But that in no ways precludes our ability to deploy risk-weighted assets profitability within the ranges that we've targeted for the business.

Fahed Kunwar: Perfect. Okay, that's all. Thank you very much.

John-Paul Crutchley, UBS

Just a couple of quick ones, but maybe just a follow-on on the capital debate. I guess I'm struck by the juxtaposition, actually, of where you are and clearly facing the uncertain road in terms of capital versus the announcement that came out of Citigroup on Friday afternoon, or Friday evening, talking about taking their Tier 1 capital ratio target down to 9.5% from 10% actually and reducing that.

And I guess the question is, when you're having the debate, the discussion with regulators and, therefore, a Group like yourself, which is clearly operating on a much broader, global stage than just a pure UK, to what degree does the old chestnut of level playing fields and actually trying to maintain the common standards actually come into that debate? Or are we, essentially, just pursuing a UK-led agenda here?

And my second, and perhaps more prosaic question, was just on the investment bank. I wonder if you could just comment on whether we should expect the normal seasonal bounce in the rates and FX business, particularly in Q1, that we've normally seen in previous years.

Stuart Gulliver: On the global banking and markets business, there does appear to be seasonality to it.

Iain Mackay: And on regulation, Douglas has been sitting here drinking coffee, so he's going to answer the question.

Stuart Gulliver: Douglas who has a doctorate in this will now (laughter) go into detail. But yes, JP, there is seasonality.

John-Paul Crutchley: Yes, okay.

Stuart Gulliver: And it's there again.

John-Paul Crutchley: Okay, understood.

Douglas Flint: I think what's playing through at the moment in global regulation is, while everybody stands up and embraces the concept of a single framework for regulation, what you're seeing is increasingly and for obvious reasons, the balkanization of capital regimes to suit the particular shape of the markets, where the regulators have, again understandably, a primary concern against their own political environment and their own taxpayer risk.

So I think it's very difficult. I don't think you would get a recognition from a regulator anywhere around the world that what they've got a responsibility to do is to create or contribute to a level playing field. I think they all believe in a set of minimum standards. They believe in as much harmonization as possible. But if they think there are steps necessary to protect their own market, or to shape the banking system within their regional market in a particular way, they will do so.

And I think the stuff that came out from Fed in the last couple of weeks on foreign banking organizations, I thought set out very, very clearly, very articulate, in terms of why was it was important. And the impact on the global economy was mentioned as being something they had taken into account, but hadn't necessarily found compelling to be a level playing field.

But for the reasons it's saying it's important for the global market that we protect the US system, and you can see why people would think like that. So yes, I think we're going to increasingly see differentials between markets, and that's just life.

John-Paul Crutchley: Thank you.

Mike Trippitt, Numis Securities

I understand the frustrations about an ROE target, when we don't know what the E's going to be. But I wonder if I could pick up on Iain's comments, I think in the answer a couple of questions ago, on return on risk assets and just get your thoughts around confidence level still to get into that.

You're at the bottom of that 2.2% to 2.6% range and I think at the time, the middle of last year, you said you're not assuming any tailwind effect from rising rates in your target range. And we've got impairments at fairly low levels, so I just wanted to understand what really drives the business on up to the 2.6% level.

And I note that GB&M you're there, by the looks of it. But in commercial banking, a way to go yet. So if you could give your thoughts around that, particularly given in the light of risk-weighted asset floors, and also just where we are in the cycle.

Iain Mackay: Mike, it's a good question. I think, if you look at the progression on risk-weighted assets over the course of the last couple of years, the businesses are making progress, quarter over quarter, in terms of pricing business comprehensively. We've moved the return on risk-weighted assets from 1.8%, this is on a reported basis, from 1.8% to 2% this year.

On an underlying basis, it's also 2%, but if you pull out the effect of the legacy run-off portfolios in GB&M and consumer portfolios in the US, that gets us to the 2.2%. And this is really a question of working one deal at a time and looking at the growth opportunities by market, differentiate by market, as Stuart described earlier, and pricing to these returns.

I think we've improved the ability within the businesses to have transparency around the risk-weighted assets and, therefore, the pricing to achieve the return on those risk-weighted assets at a much more granular level within the business. And we continue to work on that with each of the global businesses, in terms of building a more granular understanding of what really drives a) the risk-weighted assets. And then, obviously, one thing on which we've always been very conscious is how you price in the marketplace competitively to achieve some of those returns.

So again, it's not one story that -- it's not a particular rising tide that lifts all boats, but it's step by step by step, deal by deal, to work through this improving the granularity and visibility to date and then pricing competitively in the market place.

So the progress over the course of the last couple of years is encouraging and we just have to keep building on that.

Mike Trippitt: I don't know if I could just push you a little bit on the commercial banking business, though, which is sitting below your target range. Can you give some calibration around, say, if you were to go back to a more normalized -- you talked about a bottoming out on trade finance margins. If they start to normalize again, what impact do you think that you think that would on return on RWAs?

Iain Mackay: Clearly, the spread compression that we saw, particularly in Asia in the first half of this year, was marked. And I think one of the answers to an earlier question was that we still haven't seen the level of pricing that we saw at the end of 2012, in that particular space.

So we're seeing stabilization coming in. I think perhaps one of the factors that is of particular benefit to HSBC is that as we see some of the liquidity move out of this market, and some of the uncertainty around EM, which is certainly promulgated and promoted by the press, we continue to see growth opportunities across the significant majority of our markets, in emerging markets, whether it's Asia or further afield. And as that pricing stabilizes, our liquidity helps us take share, equally shown in LatAm.

So yes, the compression had a significant effect on margins, and particularly in CMB in 2013, but we'll build recovery from there as margins stabilize. It's not in our plans, but as we see interest rates, hopefully, improve over the next 18 to 24 months, that will continue to filter through.

Mike Trippitt: Thank you.

Vincent Chang, Goldman Sachs

My question is on others categories which is on page 92 of the annual report. I noticed last quarters, the first nine months of the year, the pre-tax profit was [$66 million] and it became minus [$2,145 million] for the full year. So I'm just wondering if you can give us bit breakdown on the quarter-on-quarter movement in these categories?

And then also clarify, is that $1.4 billion Panama disposal gain booked under this category? Thank you.

Iain Mackay: No, the Panama gain is booked in each business, in each global business, so it was split between commercial bank, global banking and markets and retail banking and wealth management. So it is not booked within other.

In terms of the development of operating income, I think one of the most significant features is that the bank levy is booked in other, in terms of operating expense, and that's in the fourth quarter.

And the other is the movement in fair value of own debt. Those are the key differentiating feature in terms of shall we say ongoing revenues and expenses fairly consistent.

Vincent Chang: Okay. The bank levy is $900 million, the fair value own debt is roughly $200 million I suppose? But the movement is like $2.2 billion, so I'm wondering if I miss anything there?

Iain Mackay: So the fair value and debt for the quarter was $650 million, okay? The bank levy was $907 million and ongoing operating expenses were very consistent across the quarters at about $450 million last year. So a comparison on last year we'd be including Ping An and industrial bank so that didn't come through again. So there is a lower dividend on the industrial bank in the third quarter of this year.

Vincent Chang: Okay. Thank you.

Stuart Gulliver: It was the fourth quarter. There's no industrial bank dividend in the fourth quarter, because we've reclassified it.

Vincent Chang: I see. Thank you.

Chris Wheeler, Mediobanca

Two quick questions. The first one is on slide 17, Stuart, the strategic priorities for 2014/2016. You talk about redesigning key processes. I know, talking to John Flint, that you're redesigning, reworking the retail platform. Can you also just tell us, are you working on the other two major business platforms, commercial and obviously global banking and markets? And will there be a cost to getting to the two points, to the $2 billion to $3 billion of additional cost savings you're planning on?

And the final question, just very quickly. Where are you in the derisking of the European global private banking business? Obviously, you're now keeping Monaco; you told us that last quarter. How far are you along the road to really getting the business into the shape you want, where you feel very, very comfortable with it within the terms of the six filter? Thank you.

Stuart Gulliver: Commercial banking will have the same program that John's spoken to you about in retail banking and wealth management, which Simon Cooper can give you a deep dive on. But again, commercial banking was not run as single global business really until Alan Keir began to get a grip on it in the last couple or three years. So there are still significant opportunities to harmonize processes and procedures and to get the economies of scale that a firm of our size should have.

So again, in CMB, you've got multiple Internet platforms, just as you have in retail banking and wealth management. They're just very simple things, obvious things like that, where we can get cost out.

Global banking and markets less so. It's been run as a global business since actually about 19 -- certainly since about 2003. So actually, there's less process synergy necessarily can come out of global banking and markets; it's more advanced in that regard.

As for the private bank --

Chris Wheeler: Sorry, can I ask, Stuart, is there a cost to the $2 billion to $3 billion savings or will it be lost in the normal day to day costs of the two businesses?

Stuart Gulliver: I expect it's been lost in the normal way in the costs of the two businesses. (multiple speakers)

Chris Wheeler: Okay. Thank you.

Stuart Gulliver: And then on private banking, the bulk of the restructuring of the European or the Swiss business is behind us. The business that we've restructured is obviously the Republic one. So we bought Republic Bank of New York; it had a client base that actually did not have a great deal of synergy with the rest of the HSBC Group.

And what I want to see going forward, and there was a great example in 2013, as I said earlier, of $5 billion of AuM coming from introductions from commercial banking to the private bank. I want, basically, the client base to be the client base that we always had in Singapore and Hong Kong in the private bank of the Hong Kong Shanghai Banking Corporation. Or actually, the private bank of what used to be British Bank of the Middle East in Geneva, which was the wealthy clients that we had in other parts of the Bank in the Middle East or in Asia-Pacific.

So the bulk of the restructuring of the Swiss piece is behind us. We remain committed to our private banking business; we remain committed to actually Switzerland, which is a core proposition. But what I would expect to find is that our own clients, if you like, inform most of our private banking clients, that most of our focus will be on onshore and, where we have an offshore proposition, it's on a tax transparent basis, i.e., it's on a disclosed funds basis.

So I think you should expect to see improvement in 2014, in the PBT of the private bank, from where we stand here.

Chris Wheeler: Thanks very much. That's very helpful, thank you.

Stuart Gulliver, Group Chief Executive

Thank you all for your interest. Thank you.