HSBC Bank Canada

Third Quarter 2018 Interim Report

HSBC

Third Quarter 2018 Interim Report

Highlights

For the quarter and nine months ended 30 September 2018 compared with the same periods in the prior year (unless otherwise stated).

Quarter ended 30 September:

– *Total operating income*: $588m, up $60m or 11.4%

– *Profit before income tax expense*: $271m, up $53m or 24.3%

– *Profit attributable to the common shareholder:* $189m, up $36m or 23.5%

– *Return on average common equity*[1]: 16.5% (2017: 12.7%)

Nine months ended 30 September:

– *Total operating income*: $1,699m, up $169m or 11%

– *Profit before income tax expense*: $769m, up $80m or 11.6%

– *Profit attributable to the common shareholder*: $533m, up $45m or 9.2%

– *Return on average common equity*[1]: 15.2% (2017:13.8%),

As at 30 September:

– *Total assets:* $103.7bn (31 Dec 2017: $96.4bn)

– *Common equity tier 1 capital ratio:* 11.1% (31 Dec 2017: 10.5%)

– *Tier 1 ratio:* 13.3% (31 Dec 2017: 12.4%)

– *Total capital ratio:* 15.9% (31 Dec 2017: 14.7%)

HSBC Bank Canada reported strong results for the quarter and year-to-date, with double digit growth for both total operating income and profit before income tax expense. Total operating income grew for all of our global businesses as we continue to execute our strategy and focus on growth and value creation.

Our results were driven by loan growth across all of our global businesses: Commercial Banking, Retail Banking and Wealth Management and Global Banking and Markets. Higher interest rates and increased revenue from information technology services provided to affiliated Group companies also contributed to our results.

In Commercial Banking, loan growth was at its highest level since 2010 and operating income growth was seen across most business segments. This led to an increase in operating income of $26m, or 12%, for the quarter and $59m, or 9.1%, for the year-to-date.

In Global Banking and Markets, total operating income grew by $4m, or 4.5%, for the quarter and $30m, or 13.2%, for the year-to-date, as we continued to leverage HSBC's global network to provide products and solutions to meet our global clients' needs.

In Retail Banking and Wealth Management, we continued to achieve strong growth in total relationship balances[2] and to grow market share in deposits and mortgages. This led to an increase in total operating income of $19m, or 10.9%, for the quarter and $54m, or 10.8%, for the year-to-date.

Favourable credit conditions, together with active risk management, led to a net recovery position in the change in expected credit losses[3] for both the quarter and year-to-date, although this has reduced from the elevated recovery levels experienced in 2017.

We continue to invest in growing our business and making it more convenient for our customers to bank with us, resulting in an increase in operating expenses of $20m, or 2.1%, for the year-to-date. For the quarter, operating expenses decreased by $3m, or 0.9%.

Commenting on the results, Sandra Stuart, President and Chief Executive Officer of HSBC Bank Canada, said:

"We continue to build our business and Q3 was no exception. Our team has continued to help our retail, corporate and institutional customers make the most of opportunities as they pursue their domestic and global growth ambitions. Revenues and asset growth remain strong across all of our business lines, and profit before tax is up 24.3% over the same period last year as we bring more of HSBC to Canadian customers. Our strategy is yielding results and we remain focused on our customer relationships and building business one customer at a time."

1 *For additional information, see the 'Use of non-IFRS financial measures' section of the Management's Discussion and Analysis.*
2 *Total relationship balances are comprised of lending, deposits and wealth balances.*
3 *Effective 1 January 2018 under IFRS 9 the term 'change in expected credit losses' is used. The equivalent term prior to 1 January 2018 under IAS 39 was 'loan impairment charges and other credit risk provisions'.*

Interim report contents

Management's Discussion and Analysis

HSBC Bank Canada ('the bank', 'we', 'our') is an indirectly wholly-owned subsidiary of HSBC Holdings plc ('HSBC Holdings'). Throughout the Management's Discussion and Analysis ('MD&A'), the HSBC Holdings Group is defined as the 'HSBC Group' or the 'Group'.

The MD&A is provided to enable readers to assess our financial condition and results of operations for the quarter and nine months ended 30 September 2018, compared to the same periods in the preceding year. The MD&A should be read in conjunction with our unaudited interim condensed consolidated financial statements and related notes for the quarter and nine months ended 30 September 2018 ('consolidated financial statements') and our Annual Report and Accounts 2017. This MD&A is dated 26 October 2018, the date that our consolidated financial statements and MD&A were approved by our Board of Directors ('the Board'). The references to 'notes' throughout this MD&A refer to notes on the consolidated financial statements for the quarter and nine months ended 30 September 2018.

The bank has prepared its consolidated financial statements in accordance with International Financial Reporting Standards ('IFRS') and in consideration of the accounting guidelines as issued by the Office of the Superintendent of Financial Institutions Canada ('OSFI'), as required under Section 308(4) of the *Bank Act.* The abbreviations '$m' and '$bn' represent millions and billions of Canadian dollars, respectively. All tabular amounts are in millions of dollars except where otherwise stated.

Our continuous disclosure materials, including interim and annual filings are available through a link on the bank's website at www.hsbc.ca. These documents and the 2017 Annual Information Form are also available on the Canadian Securities Administrators' website at www.sedar.com. Complete financial, operational and investor information for HSBC Holdings and the HSBC Group, including HSBC Bank Canada, can be obtained from its website, www.hsbc.com, including copies of HSBC Holdings Annual Report and Accounts 2017. Information contained in or otherwise accessible through the websites mentioned does not form part of this report.

MD&A contents

Caution regarding forward-looking statements

This document contains forward-looking information, including statements regarding the business and anticipated actions of the bank. These statements can be identified by the fact that they do not pertain strictly to historical or current facts. Forward-looking statements often include words such as 'anticipates', 'estimates', 'expects', 'projects', 'intends', 'plans', 'believes' and words and terms of similar substance in connection with discussions of future operating or financial performance. By their very nature, these statements require us to make a number of assumptions and are subject to a number of inherent risks and uncertainties that may cause actual results to differ materially from those contemplated by the forward-looking statements. We caution you to not place undue reliance on these statements as a number of risk factors could cause our actual results to differ materially from the expectations expressed in such forward-looking statements. The Risk Management section in the MD&A of our Annual Report and Accounts 2017 describes the most significant risks to which the bank is exposed and, if not managed appropriately, could have a material impact on our future financial results. These risk factors include: credit risk, liquidity and funding risk, market risk and structural interest rate risk. Additional risks that could cause our actual results to differ materially from the expectations expressed in such forward-looking statements include: operational risks (including compliance, regulatory, financial crime, security and fraud, and fiduciary risks) and reputational risks. Other factors that may cause our actual results to differ materially from the expectations expressed in such forward-looking statements include: general economic and market conditions, fiscal and monetary policies, changes in laws, regulations and approach to supervision, level of competition and disruptive technology, changes to our credit rating, and operational and infrastructure risks. Refer to the 'Factors that may affect future results' section of our Annual Report and Accounts 2017 for a description of these risk factors. We caution you that the risk factors disclosed above are not exhaustive, and there could be other uncertainties and potential risk factors not considered here which may adversely affect our results and financial condition. Any forward-looking statements in this document speak only as of the date of this document. We do not undertake any obligation to, and expressly disclaim any obligation to, update or alter our forward-looking statements, whether as a result of new information, subsequent events or otherwise, except as required under applicable securities legislation.

Management's Discussion and Analysis (continued)

Who are we

HSBC Bank Canada is the leading international bank in the country. We help companies and individuals across Canada to do business and manage their finances internationally through three global businesses: Commercial Banking, Global Banking and Markets, and Retail Banking and Wealth Management. No international bank has our Canadian presence and no domestic bank has our international reach.

Canada is an important contributor to the HSBC Group growth strategy and a key player in HSBC's work to support customers and drive growth, leveraging its footprint across all key trade corridors, including in North America, alongside the United States and Mexico, and with China.

The HSBC Group is one of the world's largest banking and financial services groups with assets of US$2,603bn at 30 September 2018. HSBC serves customers worldwide through an international network of about 3,800 offices in 66 countries and territories in Europe, Asia, North and Latin America, and the Middle East and North Africa.

Throughout HSBC's history we have been where the growth is, connecting customers to opportunities, enabling businesses to thrive and economies to prosper, helping people fulfil their hopes and dreams and realize their ambitions.

Shares in HSBC Holdings are listed on the London, Hong Kong, New York, Paris and Bermuda stock exchanges. The shares are traded in New York in the form of American Depositary Receipts.

Use of non-IFRS financial measures

In measuring our performance, the financial measures that we use include those which have been derived from our reported results. However, these are not presented within the consolidated financial statements and are not defined under IFRS. These are considered non-IFRS financial measures and are unlikely to be comparable to similar measures presented by other companies. The following non-IFRS financial measures are used throughout this document.

Return on average common shareholder's equity is calculated as annualized profit attributable to the common shareholder for the period divided by average[1] common equity.

Return on average risk-weighted assets is calculated as the annualized profit before income tax expense divided by the average[1] risk-weighted assets.

Cost efficiency ratio is calculated as total operating expenses as a percentage of total operating income.

Operating leverage/jaws is calculated as the difference between the rates of change for revenue and operating expenses.

Net interest margin is net interest income expressed as an annualized percentage of average[1] interest earning assets.

Change in expected credit losses to average gross loans and advances and acceptances is calculated as the annualized change in expected credit losses[2] as a percentage of average[1] gross loans and advances to customers and acceptances.

Change in expected credit losses on stage 3 loans and advances and acceptances to average gross loans and advances and acceptances is calculated as the annualized change in expected credit losses[2] on stage 3[2] assets as a percentage of average[1] gross loans and advances to customers and acceptances.

Total stage 3 allowance for expected credit losses to gross stage 3 loans and advances and acceptances is calculated as the total allowance for expected credit losses relating to stage 3[2] loans and advances to customers and acceptances as a percentage of stage 3[2] loans and advances to customers and acceptances.

Net write-offs as a percentage of average customer advances and acceptances is calculated as annualized net write-offs as a percentage of average[1] net customer advances and acceptances.

1 *Average balances are calculated using month-end balances.*

2 *Effective 1 January 2018 under IFRS 9 the terms 'change in expected credit losses' and 'stage 3 assets' are used. The equivalent terms prior to 1 January 2018 under IAS 39 are 'loan impairment charges and other credit risk provisions' and 'impaired assets' respectively.*

Financial Highlights

($ millions, except where otherwise stated)	Quarter ended		Nine months ended	
	30 Sep 2018[1]	30 Sep 2017	**30 Sep 2018**[1]	30 Sep 2017
Financial performance for the period				
Total operating income	**588**	528	**1,699**	1,530
Profit before income tax expense	**271**	218	**769**	689
Profit attributable to the common shareholder	**189**	153	**533**	488
Change in expected credit losses -recovery	**7**	n/a	**46**	n/a
Loan impairment recoveries and other credit risk provisions	**n/a**	14	**n/a**	109
Operating expenses	**(324)**	(327)	**(976)**	(956)
Basic and diluted earnings per common share ($)	**0.38**	0.31	**1.07**	0.98
Financial measures[2]				
Return on average common shareholder's equity (%)	**16.5**	12.7	**15.2**	13.8
Return on average risk-weighted assets[3,4] (%)	**2.7**	2	**2.5**	2.1
Cost efficiency ratio (%)	**55.1**	61.9	**57.4**	62.5
Operating leverage/jaws (%)	**12.3**	6.3	**9**	(5.2)
Net interest margin (%)	**1.59**	1.48	**1.54**	1.47
Change in expected credit losses to average gross loans and advances and acceptances[5] (%)	**n/a**	n/a	**n/a**	n/a
Change in expected credit losses on stage 3 loans and advances and acceptances to average gross loans and advances and acceptances[5] (%)	**n/a**	—	**n/a**	n/a
Total stage 3 allowance for expected credit losses to gross stage 3 loans and advances and acceptances[5] (%)	**36.9**	39.6	**36.9**	39.6
Net write-offs as a percentage of average loans and advances and acceptances (%)	**0.10**	0.12	**0.14**	0.13

	At period ended	
	30 Sep 2018[1]	31 Dec 2017
Financial position at period end		
Total assets	**103,677**	96,379
Loans and advances to customers	**54,114**	50,337
Customer accounts	**57,982**	57,054
Ratio of loans and advances to customer accounts (%)	**93.3**	88.2
Common shareholder's equity	**4,576**	4,860
Capital measures[3]		
Common equity tier 1 capital ratio ('CET1') (%)	**11.1**	10.5
Tier 1 ratio (%)	**13.3**	12.4
Total capital ratio (%)	**15.9**	14.7
Leverage ratio (%)	**4.5**	4.9
Risk-weighted assets[4]	**39,618**	45,035
Liquidity coverage ratio (%)	**135**	137

1 *Effective 1 January 2018 the bank adopted IFRS 9 Financial Instruments ('IFRS 9') on a retrospective basis without restatement of prior periods. Results from prior periods are reported in accordance with IAS 39 Financial Instruments: Recognition and Measurement ('IAS 39').*

2 *Refer to the 'Use of non-IFRS financial measures' section of this document for a discussion of non-IFRS financial measures.*

3 *The bank assesses capital adequacy against standards established in guidelines issued by OFSI in accordance with the Basel III capital adequacy framework.*

4 *In January 2018, OSFI announced its decision to update the existing capital floor for institutions using advanced approaches for credit risk and operational risk. Effective from the second quarter of 2018, the capital floor was based on the Standardized approach under Basel II framework with the floor factor transitioned in over three quarters. The floor factor was set at 70% for the second quarter of 2018, increasing to 72.5% in the third quarter of 2018 and 75% in the fourth quarter of 2018.*

5 *Effective 1 January 2018 under IFRS 9 the terms 'change in expected credit losses' and 'stage 3 assets' are used. The equivalent terms prior to 1 January 2018 under IAS 39 were 'loan impairment charges and other credit risk provisions' and 'impaired assets' respectively. n/a is shown where the bank is in a net recovery position resulting in a negative ratio.*

Management's Discussion and Analysis (continued)

Financial performance

Summary consolidated income statement

	Quarter ended		Nine months ended	
	30 Sep 2018[1]	30 Sep 2017	**30 Sep 2018[1]**	30 Sep 2017
	$m	$m	**$m**	$m
Net interest income	**332**	292	**957**	859
Net fee income	**175**	169	**509**	494
Net income from financial instruments held for trading (2017: Net trading income)	**35**	41	**110**	94
Other items of income	**46**	26	**123**	83
Total operating income	**588**	528	**1,699**	1,530
Change in expected credit losses- recovery	**7**	n/a	**46**	n/a
Loan impairment recoveries and other credit risk provisions	**n/a**	14	**n/a**	109
Net operating income	**595**	542	**1,745**	1,639
Total operating expenses	**(324)**	(327)	**(976)**	(956)
Operating profit	**271**	215	**769**	683
Share of profit in associates	**—**	3	**—**	6
Profit before income tax expense	**271**	218	**769**	689
Income tax expense	**(73)**	(56)	**(208)**	(173)
Profit for the period	**198**	162	**561**	516

1 *Effective 1 January 2018 the bank adopted IFRS 9 on a retrospective basis without restatement of prior periods. Results from prior periods are reported in accordance with IAS 39.*

Performance by income and expense item

For the quarter and nine months ended 30 September 2018 compared with the same periods in the prior year.

Net interest income

Net interest income increased by $40m, or 13.7%, for the quarter and by $98m, or 11.4%, for the year-to date. Contributing to the increase for both the quarter and the year-to-date were volume growth in both lending and deposits within Retail Banking and Wealth Management, in particular residential mortgage balances and personal deposits, and higher loans and advances in Commercial Banking. In addition, we benefited from improved margins as a result of higher interest rates. This was partially offset by lower interest from impaired loans.

Summary of interest income by types of assets

	Quarter ended						Nine months ended					
	30 Sep 2018[1]			30 Sep 2017[2]			**30 Sep 2018[1]**			30 Sep 2017[2]		
	Average balance	**Interest income**	**Yield**	Average balance	Interest income	Yield	**Average balance**	**Interest income**	**Yield**	Average balance	Interest income	Yield
	$m	**$m**	**%**	$m	$m	%	**$m**	**$m**	**%**	$m	$m	%
Interest income												
Short-term funds and loans and advances to banks	**736**	**—**	**0.02**	1,102	1	0.36	**810**	**3**	**0.50**	1,161	2	0.28
Loans and advances to customers	**50,268**	**485**	**3.83**	48,015	398	3.28	**51,758**	**1,344**	**3.47**	46,864	1,146	3.27
Reverse repurchase agreements - non-trading	**7,693**	**32**	**1.63**	7,820	17	0.86	**6,682**	**82**	**1.63**	7,687	41	0.71
Financial investments	**23,747**	**113**	**1.88**	21,426	65	1.21	**23,505**	**316**	**1.80**	22,262	195	1.17
Other interest-earning assets	**286**	**1**	**1.21**	—	—	—	**308**	**2**	**0.81**	—	—	—
Total interest-earning assets *(A)*	**82,730**	**631**	**3.03**	78,363	481	2.44	**83,063**	**1,747**	**2.81**	77,974	1,384	2.37
Trading assets and financial assets designated at fair value[3]	**4,671**	**24**	**2.07**	5,119	18	1.37	**5,042**	**76**	**2.00**	6,208	50	1.08
Non-interest-earning assets	**14,868**	**—**	**—**	11,479	—	—	**11,411**	**—**	**—**	11,157	—	—
Total	**102,269**	**655**	**2.54**	94,961	499	2.08	**99,516**	**1,823**	**2.45**	95,339	1,434	2.01

Summary of interest expense by type of liabilities and equity

	Quarter ended						Nine months ended					
	30 Sep 2018[1]			30 Sep 2017[2]			**30 Sep 2018[1]**			30 Sep 2017[2]		
	Average balance	**Interest expense**	**Cost**	Average balance	Interest expense	Cost	**Average balance**	**Interest expense**	**Cost**	Average balance	Interest expense	Cost
	$m	**$m**	**%**	$m	$m	%	**$m**	**$m**	**%**	$m	$m	%
Interest expense												
Deposits by banks[4]	**1,087**	**1**	**0.23**	1,120	1	0.08	**928**	**2**	**0.24**	957	1	0.10
Financial liabilities designated at fair value - own debt issued	**—**	**—**	**—**	—	—	—	**—**	**—**	**—**	146	1	1.22
Customer accounts[5]	**51,553**	**163**	**1.25**	49,000	100	0.81	**51,059**	**436**	**1.14**	49,218	278	0.76
Repurchase agreements - non-trading	**8,109**	**35**	**1.70**	4,866	10	0.85	**7,311**	**88**	**1.61**	5,384	29	0.73
Debt securities in issue and subordinated debt	**13,925**	**89**	**2.54**	10,977	63	2.25	**12,607**	**234**	**2.48**	10,518	172	2.18
Other interest-bearing liabilities	**1,771**	**11**	**2.57**	2,986	15	1.94	**1,763**	**30**	**2.31**	2,410	44	2.43
Total interest bearing liabilities *(B)*	**76,445**	**299**	**1.55**	68,949	189	1.09	**73,668**	**790**	**1.43**	68,633	525	1.02
Trading liabilities and financial liabilities designated at fair value (excluding own debt issued)[3]	**3,013**	**16**	**2.13**	3,277	13	1.58	**2,876**	**46**	**2.15**	3,595	35	1.30
Non-interest bearing current accounts	**5,996**	**—**	**—**	6,179	—	—	**6,099**	**—**	**—**	6,146	—	—
Total equity and other non-interest bearing liabilities	**16,816**	**—**	**—**	16,556	—	—	**16,872**	**—**	**—**	16,965	—	—
Total	**102,270**	**315**	**1.22**	94,961	202	0.84	**99,515**	**836**	**1.12**	95,339	560	0.79
Net interest income *(A-B)*		**332**			292			**957**			859	

1 *Effective 1 January 2018 the bank adopted IFRS 9 on a retrospective basis without restatement of prior periods. Results from prior periods are reported in accordance with IAS 39. Refer to the table 'Reconciliation of consolidated balance sheet as at 31 December 2017 and 1 January 2018' in note 1 of the consolidated financial statements for further details of balance sheet presentation changes.*
2 *Certain prior period amounts have been reclassified to conform to the current period presentation.*
3 *Interest income and expense on trading assets and liabilities is reported as `Net income from financial instruments held for trading' in the consolidated income statement.*
4 *Includes interest-bearing bank deposits only.*
5 *Includes interest-bearing customer accounts only.*

Net fee income

	Quarter ended		Nine months ended	
	30 Sep 2018	30 Sep 2017[1]	**30 Sep 2018**	30 Sep 2017[1]
	$m	$m	**$m**	$m
Account services	**14**	16	**48**	49
Broking income	**2**	2	**7**	6
Cards	**16**	14	**45**	40
Credit facilities	**73**	69	**214**	201
Funds under management	**49**	47	**144**	142
Imports/exports	**3**	2	**8**	7
Insurance agency commission	**1**	2	**4**	6
Other	**13**	10	**38**	33
Remittances	**8**	8	**25**	23
Underwriting	**16**	17	**40**	40
Fee income	**195**	187	**573**	547
Less: fee expense	**(20)**	(18)	**(64)**	(53)
Net fee income	**175**	169	**509**	494

1 *Certain prior period amounts have been reclassified to conform to the current period presentation.*

Management's Discussion and Analysis (continued)

Net fee income increased by $6m, or 3.6%, for the quarter and $15m, or 3%, for the year-to-date. The growth in fee income for both the quarter and the year-to-date were driven by higher volumes for credit facility fees, fees generated from funds under management and credit card fees. This was partially offset by an increase in fee expenses, primarily relating to enhanced credit card rewards and incentives together with higher trustee and investment advisory fees.

Net income from financial instruments held for trading

	Quarter ended		Nine months ended	
	30 Sep 2018	30 Sep 2017	**30 Sep 2018**	30 Sep 2017
	$m	$m	**$m**	$m
Trading activities	**24**	33	**74**	78
Credit valuation, debit valuation, and funding fair value adjustments	**4**	1	**5**	2
Net interest from trading activities	**8**	5	**30**	15
Hedge ineffectiveness	**(1)**	2	**1**	(1)
Net income from financial instruments held for trading (2017: Net trading income)	**35**	41	**110**	94

Net income from financial instruments held for trading for the quarter decreased by $6m, or 14.6%. Contributing to the decrease was lower income from trading activities due to accounting volatility from balance sheet management activities. In addition, hedge ineffectiveness led to a modest loss in the current quarter compared to a modest gain for the same period in the prior year.

Net income from financial instruments held for trading for the year-to-date increased by $16m, or 17%, primarily due to earning higher net interest from trading activities from higher yields. This was partially offset by the loss relating to accounting volatility as noted for the quarter.

Other items of income

	Quarter ended		Nine months ended	
	30 Sep 2018	30 Sep 2017	**30 Sep 2018**	30 Sep 2017
	$m	$m	**$m**	$m
Changes in fair value of long-term debt (2017: Net expense from financial instruments designated at fair value)	**—**	—	**—**	(4)
Gains less losses from financial investments	**18**	4	**45**	25
Dividend income	**1**	—	**1**	—
Other operating income	**27**	22	**77**	62
Other items of income	**46**	26	**123**	83

Other items of income increased by $20m, or 76.9%, for the quarter and $40m, or 48.2%, for the year-to-date. The increase for both the quarter and the year-to-date was primarily due to higher gains on the disposal of financial investments arising from the re-balancing of the bank's liquid asset portfolio, and higher income from HSBC Group entities for information technology services performed by the bank.

Change in expected credit losses[1]

	Quarter ended	Nine months ended
	30 Sep 2018[1]	**30 Sep 2018[1]**
	$m	**$m**
Change in expected credit loss- performing loans (stage 1 and 2) - (recovery)	**(1)**	**(4)**
Change in expected credit loss- non-performing loans (stage 3) - (recovery)	**(6)**	**(42)**
Change in expected credit loss - (recovery)	**(7)**	**(46)**

IAS 39 comparative

	Quarter ended	Nine months ended
	30 Sep 2017[1]	30 Sep 2017[1]
	$m	$m
Collectively assessed recoveries	(15)	(34)
Individually assessed recoveries	—	(39)
Loan impairment recoveries	(15)	(73)
Other credit risk provisions	1	(36)
Net loan impairment recoveries and other credit risk provisions	(14)	(109)

1 *Effective 1 January 2018 the bank adopted IFRS 9 on a retrospective basis without restatement of prior periods. Results from prior periods are reported in accordance with IAS 39.*

The change in expected credit losses for the quarter was a recovery of $7m compared with loan impairment recoveries and other credit risk provisions of $14m for the same period in the prior year.

The recovery in the current quarter is primarily as a result of provision releases of $6m in the non-performing portfolio from improving credit conditions primarily relating to specific energy services and manufacturing customers. This was partially offset by a charge in the non-performing portfolio in Retail Banking and Wealth Management of $2m as a result of write-offs.

The change in expected credit losses for the year-to-date was a recovery of $46m compared with loan impairment recoveries and other credit risk provisions of $109m for the same period of the prior year. The recovery in the current year was driven by credit quality improvements in the non–performing portfolio, most notably in the energy services, manufacturing and real estate sectors, which led to recoveries and transfers to the performing portfolio. These recoveries were partially offset by charges against specific clients in the construction and manufacturing industry.

The elevated recoveries in 2017 were driven by significant reversals of specific provisions in the oil and gas industry, as well as releases in collective provisions, reflecting overall improvements in credit quality.

Total operating expenses

	Quarter ended		Nine months ended	
	30 Sep 2018	30 Sep 2017	**30 Sep 2018**	30 Sep 2017
	$m	$m	**$m**	$m
Employee compensation and benefits	**179**	183	**539**	537
General and administrative expenses	**131**	134	**401**	388
Depreciation of property, plant and equipment	**8**	7	**24**	23
Amortization of intangible assets	**6**	3	**12**	8
Total operating expenses	**324**	327	**976**	956

Total operating expenses were broadly unchanged for the quarter- a decrease of $3m, or 0.9%. Total operating expenses for the year-to-date increased by $20m, or 2.1%. Contributing to the year-to-date increase was higher costs associated with the provision of information technology services to Group companies, with a related recovery increasing other operating income. In addition, employee compensation and benefits increased in our global businesses as we continue to invest to grow. This was partially offset by lower operating expenses in the Corporate Centre as certain transformation and streamlining initiatives undertaken from 2015 to 2017 are now complete. We also benefited from lower costs related to a reduction in our office space.

Share of profit/loss in associates

Share of profit/loss in associates for the quarter and year-to-date was nil compared with a gain of $3m and $6m in the prior year. The share of profits represents changes in the value of the bank's investments in private equity funds.

Income taxes expense

The effective tax rate in the third quarter of 2018 was 27.1%, which is close to the statutory tax rate. The effective tax rate for the third quarter of 2017 was 25.7%.

Management's Discussion and Analysis (continued)

Movement in financial position

Summary consolidated balance sheet	30 Sep 2018[1]	31 Dec 2017
	$m	$m
ASSETS		
Cash and balances at central bank	**69**	411
Trading assets	**4,008**	5,373
Derivatives	**3,413**	3,675
Loans and advances	**55,462**	51,558
Reverse repurchase agreements – non-trading	**7,765**	6,153
Financial investments	**23,978**	22,913
Customers' liability under acceptances	**5,627**	4,801
Other assets	**3,355**	1,495
Total assets	**103,677**	96,379
LIABILITIES AND EQUITY		
Liabilities		
Deposits by banks	**1,110**	1,696
Customer accounts	**57,982**	57,054
Repurchase agreements – non-trading	**8,793**	4,604
Trading liabilities	**1,634**	3,701
Derivatives	**3,202**	3,516
Debt securities in issue	**13,345**	10,820
Acceptances	**5,635**	4,801
Other liabilities	**6,550**	4,477
Total liabilities	**98,251**	90,669
Total equity	**5,426**	5,710
Total liabilities and equity	**103,677**	96,379

1 *Effective 1 January 2018 the bank adopted IFRS 9 on a retrospective basis without restatement of prior periods. Results from prior periods are reported in accordance with IAS 39. Refer to the table "Reconciliation of consolidated balance sheet as at 31 December 2017 and 1 January 2018" in note 1 of the consolidated financial statements for further details of balance sheet presentation changes.*

Assets

Total assets at 30 September 2018 were $103.7bn, an increase of $7.3bn, or 7.6%, from 31 December 2017. The increase in assets is mainly due to strong growth in loans and advances of $3.9bn, across all of our global businesses. Commercial Banking lending balances grew at the highest level since 2010 and Retail Banking and Wealth Management reported strong residential mortgage growth.

Other assets increased by $1.9bn primarily relating to higher unsettled balances at the period-end, and presentation changes[1] compared with the prior year. Increased reverse repurchase activity led to growth of $1.6bn and balance sheet management activities led to growth of $1.1bn in financial investments.

These increases in assets were partially offset by a reduction in trading assets of $1.4bn due to a reduction in trading debt securities held and presentation changes[1].

Liabilities

Total liabilities at 30 September 2018 were $98.3bn, an increase of $7.6bn, or 8.4%, from 31 December 2017. Higher repurchase volumes and balance sheet management activities led to an increase in non-trading repurchase agreements of $4.2bn. Debt securities in issue increased by $2.5bn, primarily due to the new issuance of medium term notes during the year. Other liabilities increased by $2.1bn, primarily due to an increase in settlement account balances at the period end.

Customer accounts increased by $1bn primarily as a result of successful campaigns run in Retail Banking and Wealth Management, partially offset by a decline in Commercial Banking deposits due to expected seasonal reductions and the impact of the US Tax reforms and resulting repatriation of balances to the US.

The increases discussed above were partially offset by a reduction in trading liabilities of $2.1bn due to lower short positions held at period end and presentation changes[1].

Equity

Total equity at 30 September 2018 was $5.4bn, a decrease of $0.3bn from 31 December 2017. Contributing to the decrease were dividends paid on common and preferred shares of $768m. In addition, a loss was reported in the financial assets at fair value through other comprehensive income reserve of $107m, primarily relating to higher interest rates and the recycling of gains to the income statement on the disposal of securities. This was partially offset by profits generated in the period of $561m.

1 *Refer to the table 'Reconciliation of consolidated balance sheet as at 31 December 2017 and 1 January 2018' in note 1 for further details of balance sheet presentation changes.*

Global businesses

We manage and report our operations around the following global businesses: Commercial Banking, Global Banking and Markets, and Retail Banking and Wealth Management.

Commercial Banking

Commercial Banking offers a full range of commercial financial services and tailored solutions to customers ranging from small and medium-sized enterprises to publicly quoted companies.

Summary income statement	Quarter ended		Nine months ended	
	30 Sep 2018[1]	30 Sep 2017	**30 Sep 2018**[1]	30 Sep 2017
	$m	$m	**$m**	$m
Net interest income	**150**	132	**434**	395
Non-interest income	**92**	84	**273**	253
Total operating income	**242**	216	**707**	648
Change in expected credit losses - recovery	**3**	n/a	**50**	n/a
Loan impairment recoveries and other credit risk provisions	**n/a**	4	**n/a**	90
Net operating income	**245**	220	**757**	738
Total operating expenses	**(104)**	(98)	**(309)**	(287)
Profit before income tax expense	**141**	122	**448**	451

1 *Effective 1 January 2018 the bank adopted IFRS 9 on a retrospective basis without restatement of prior periods. Results from prior periods are reported in accordance with IAS 39.*

Review of financial performance[1]

Overview

Total operating income in Commercial Banking increased by $26m, or 12%, for the quarter and $59m, or 9.1%, for the year-to-date. Growth was seen across most business segments, and was most notable in the Ontario region, Commercial Real Estate and International Subsidiary Banking.

Building on the expansion started in 2017 we have invested in sales transformation and streamlined processes to increase customer acquisition and product penetration, and improve our position in key trade corridors. Customers are recognizing the value of our efforts: lending balances grew at the highest level since 2010; and our customer survey has shown marked improvement, with 71% of customers rating the onboarding journey as Excellent in July 2018, compared with 36% in December 2017.

Profit before income tax increased by $19m, or 15.6%, for the quarter, driven by higher operating income. Profit before income tax decreased by $3m, or 0.7%, for the year-to-date, as higher operating income was more than offset by lower loan impairment recoveries and higher operating expenses to drive business growth.

Financial performance by income and expense item

Net interest income for the quarter and year-to-date increased by $18m, or 13.6%, and $39m, or 9.9%, respectively. The growth reflects higher loans and advances from new and existing customers and improved margins from interest rate increases. This was partly offset by lower interest recoveries on impaired loans. Deposit balances were also lower due to portfolio transfers between global businesses[2], expected seasonal reductions, and the impact of the US Tax reforms and resulting repatriation of balances to the US.

Non-interest income for the quarter and year-to-date increased by $8m, or 9.5%, and $20m, or 7.9%, respectively. The increase for both the quarter and year-to-date was primarily due to higher bankers acceptance balances, as well as higher foreign exchange and interest rate swaps revenue.

Change in expected credit losses for the quarter resulted in a recovery of $3m. This was primarily a result of provision releases from improving credit conditions for specific energy services customers. The change in expected credit losses for the year-to-date was a recovery of $50m. This was driven by the continuing improvements in several sectors, most notably the energy services sector.

Loan impairment recoveries and other credit risk provisions under IAS 39 for the prior year resulted in a recovery of $4m and $90m for the quarter and year-to-date respectively, driven by improving credit conditions, primarily from exposures in the oil and gas industry.

Total operating expenses for the quarter and year-to-date increased by $6m, or 6.1%, and $22m, or 7.7%, respectively. The increase for both the quarter and year-to-date reflects planned investments in our technology and people to better serve our customers and grow market share in support of our strategic plan.

1 *For the quarter and nine months ended 30 September 2018 compared with the same periods in the prior year.*

2 *Effective 1 January 2018, $696m of Customer accounts from Commercial Banking were reclassified to Retail Banking and Wealth Management.*

Management's Discussion and Analysis (continued)

Global Banking and Markets

Global Banking and Markets provides tailored financial solutions to major government, corporate and institutional clients worldwide.

Summary income statement	Quarter ended		Nine months ended	
	30 Sep 2018[1]	30 Sep 2017	**30 Sep 2018**[1]	30 Sep 2017
	$m	$m	**$m**	$m
Net interest income	**30**	28	**79**	74
Non-interest income	**63**	61	**178**	153
Total operating income	**93**	89	**257**	227
Change in expected credit losses - (charge)	**—**	n/a	**(1)**	n/a
Loan impairment recoveries and other credit risk provisions	**n/a**	8	**n/a**	13
Net operating income	**93**	97	**256**	240
Total operating expenses	**(39)**	(33)	**(116)**	(100)
Profit before income tax expense	**54**	64	**140**	140

1 *Effective 1 January 2018 the bank adopted IFRS 9 on a retrospective basis without restatement of prior periods. Results from prior periods are reported in accordance with IAS 39.*

Review of financial performance[1]

Overview

Global Banking and Markets total operating income increased by $4m, or 4.5%, for the quarter. The increase was mainly due to infrastructure debt capital markets transactions. Total operating income for the year-to-date increased by $30m, or 13.2%, driven by increased infrastructure debt capital markets transactions, increased interest rates, and higher sales and trading in rates and foreign exchange products.

We continue to leverage HSBC's global network to provide products and solutions to meet our global clients' needs. We have also increased the scale of our Multinational business by improving product penetration with existing customers.

Profit before income tax expense for the quarter decreased by $10m, or 15.6%. For the year-to-date, profit before income tax was $140m, unchanged from the prior year. The decrease in the quarter was driven by higher loan impairment recoveries in the prior year together with higher costs in the current quarter relating to investments in Global Banking client coverage and risk and compliance initiatives. This was partially offset by higher operating income.

Financial performance by income and expense item

Net interest income for the quarter and year-to-date increased by $2m, or 7.1% and $5m, or 6.8%, respectively. The increase for both the quarter and year-to-date was mainly due to the Bank of Canada interest rate increases in 2017 and 2018.

Non-interest income for the quarter increased by $2m, or 3.3%. This was primarily due to higher infrastructure debt capital markets fees. Non-interest income for the year-to-date increased by $25m, or 16.3%. The was primarily due to higher sales and trading activities in foreign exchange and rates products and infrastructure debt capital markets transactions.

Change in expected credit losses were nil for the quarter compared with loan impairment recoveries and other credit risk provisions of $8m in the prior year. Change in expected credit losses for the year-to-date was a charge of $1m compared with loan impairment recoveries and other credit risk provisions of $13m in the prior year. Recoveries in the prior year were a result of the continued improvements in the oil and gas industry. The current year amount includes a specific provision in the non-performing portfolio relating to the construction industry.

Total operating expenses for the quarter and year-to-date increased by $6m, or 18.2%, and $16m, or 16%, respectively as we invested in Global Banking client coverage and risk and compliance initiatives.

1 *For the quarter and nine months ended 30 September 2018 compared with the same periods in the prior year.*

Retail Banking and Wealth Management

Retail Banking and Wealth Management offers a full range of competitive banking products and services for all Canadians to help them manage their finances and protect and build for their financial future.

Summary income statement	Quarter ended		Nine months ended	
	30 Sep 2018[1]	30 Sep 2017	**30 Sep 2018**[1]	30 Sep 2017
	$m	$m	**$m**	$m
Net interest income	**129**	111	**363**	311
Non-interest income	**64**	63	**189**	187
Total operating income	**193**	174	**552**	498
Change in expected credit losses - recovery/(charge)	**4**	n/a	**(3)**	n/a
Loan impairment recoveries and other credit risk provisions	**n/a**	2	**n/a**	6
Net operating income	**197**	176	**549**	504
Total operating expenses	**(158)**	(160)	**(488)**	(453)
Profit before income tax expense	**39**	16	**61**	51
Ongoing Retail Banking and Wealth Management business	***36***	*10*	***52***	*34*
Run-off consumer finance portfolio	***3***	*6*	***9***	*17*
Profit before income tax expense	***39***	*16*	***61***	*51*

1 *Effective 1 January 2018 the bank adopted IFRS 9 on a retrospective basis without restatement of prior periods. Results from prior periods are reported in accordance with IAS 39.*

Review of financial performance[1]

Overview

Total operating income in Retail Banking and Wealth Management increased for both the quarter and year-to-date by $19m, or 10.9%, and $54m, or 10.8%, respectively. We continued to achieve strong growth in total relationship balances[2] and to grow market share primarily in deposits and mortgages, due to strong branding, innovation and strategic investments to make our bank simpler, faster and better for our clients.

During the quarter, we introduced competitive qualification criteria for customers in our Advance proposition, launched a Mortgage Centre to better serve our customers, and waived our foreign exchange fees on outgoing transfers up to a certain limit. We also continued to invest in digital technologies, for example, we launched HSBC Wealth Compass™, a simple way to receive advice and invest online, improved our mobile banking app, automated mortgage renewals to reduce processing time and introduced online originations of credit cards to all customers.

Profit before income tax expense increased by $23m, or 143.8%, for the quarter, due to higher revenue from business growth and higher interest rates. Profit before income tax expense increased by $10m, or 19.6%, for the year-to-date due to higher revenues, partly offset by continued investments and the higher cost base associated with our enhanced service model, and the growth already achieved. For example, we continued to invest in the roll-out of retail business banking, unsecured lending and Jade, an exclusive service for high-net-worth customers.

Profit before income tax expense relating to the run-off consumer finance portfolio for the quarter and year-to-date decreased by $3m, or 50%, and $8m, or 47.1%, respectively. The decrease was due to lower interest income from declining loan balances and lower expected credit loss recoveries.

Financial performance of the ongoing business by income and expense item

Net interest income for the quarter and year-to-date increased by $19m, or 17.8%, and $55m, or 18.4%, respectively. The increase for both the quarter and year-to-date was primarily due to improved margins on deposits and growth in both lending and deposits balances.

Non-interest income for the third quarter and for the first nine months of 2018 was $64m and $189m, respectively, marginally higher compared with the same periods in the prior year.

Change in expected credit losses resulted in recovery of $3m for the quarter and charges of $6m for the year-to-date. The movements in the expected credit losses were primarily due to increased volatility experienced under IFRS 9 due to forward looking economic factors.

Loan impairment charges and other credit provisions for the third quarter and for the first nine months of 2017 were $1m and $3m, respectively.

Total operating expenses for the quarter were $157m, unchanged compared with the prior year. Total operating expenses for the year-to-date were $485m, an increase of $37m, or 8.3%. This was primarily due to strategic investments to grow our business although at a more modest pace than in past quarters. The higher cost base associated with offering an enhanced service model to our growing client base continues to have an impact on costs.

1 *For the quarter and nine months ended 30 September 2018 compared with the same periods in the prior year.*

2 *Total relationship balances is comprised of lending, deposits and wealth balances.*

Management's Discussion and Analysis (continued)

Corporate Centre

Corporate Centre contains Balance Sheet Management, interests in associates and joint ventures, the results of movements in the fair value of our own debt, and income related to information technology services provided to HSBC Group companies which do not directly relate to our global businesses.

Summary income statement	Quarter ended		Nine months ended	
	30 Sep 2018[1]	30 Sep 2017	**30 Sep 2018**[1]	30 Sep 2017
	$m	$m	**$m**	$m
Net interest income	**23**	21	**81**	79
Non-interest income	**37**	28	**102**	78
Net operating income	**60**	49	**183**	157
Total operating expenses	**(23)**	(36)	**(63)**	(116)
Operating profit	**37**	13	**120**	41
Share of profit in associates	**—**	3	**—**	6
Profit before income tax expense	**37**	16	**120**	47

1 *Effective 1 January 2018 the bank adopted IFRS 9 on a retrospective basis without restatement of prior periods. Results from prior periods are reported in accordance with IAS 39.*

Review of financial performance[1]

Net operating income increased by $11m, or 22.4%, for the quarter and $26m, or 16.6%, for the year-to-date.

Contributing to the increase in both the quarter and year-to-date are gains from the disposal of securities as part of balance sheet management activities and increased revenue for information technology services provided to affiliated Group companies, with a related increased in operating expenses.

This was partly offset by a decline in net income from financial instruments held for trading due to a number of smaller movements together with impact of accounting volatility from balance sheet management activities.

Operating expenses decreased $13m, or 36.1 %, for the quarter and $53m, or 45.7%, for the year-to-date, as we completed certain transformation and streamlining initiatives undertaken from 2015 to 2017.

The impact of these movements was an increase in profit before income tax of $21m for the quarter and $73m for the year-to-date.

1 *For the quarter and nine months ended 30 September 2018 compared with the same periods in the prior year.*

Summary quarterly performance

The following table provides summary information related to the Bank's eight most recently completed quarters.

Summary consolidated income statement

	Quarter ended							
	30 Sep 2018[1]	30 Jun 2018[1]	31 Mar 2018[1]	31 Dec 2017	30 Sep 2017	30 June 2017	31 Mar 2017	31 Dec 2016
	$m	$m	$m	$m	$m	$m	$m	$m
Net interest income	**332**	319	306	318	292	285	282	282
Net fee income	**175**	179	155	159	169	165	160	169
Net income from financial instruments held for trading (2017: Net trading income)	**35**	39	36	31	41	22	31	45
Other items of income	**46**	33	44	32	26	24	33	16
Total operating income	**588**	570	541	540	528	496	506	512
Change in expected credit losses	**7**	11	28	n/a	n/a	n/a	n/a	n/a
Loan impairment (charges)/recoveries and other credit risk provisions	**n/a**	n/a	n/a	(1)	14	46	49	61
Net operating income	**595**	581	569	539	542	542	555	573
Total operating expenses	**(324)**	(334)	(318)	(333)	(327)	(318)	(311)	(325)
Operating profit	**271**	247	251	206	215	224	244	248
Share of profit/(loss) in associates	**—**	—	—	—	3	4	(1)	3
Profit before income tax expense	**271**	247	251	206	218	228	243	251
Income tax expense	**(73)**	(67)	(68)	(54)	(56)	(60)	(57)	(63)
Profit for the period	**198**	180	183	152	162	168	186	188
Profit attributable to common shareholder	**189**	171	173	142	153	158	177	178
Profit attributable to preferred shareholders	**9**	9	10	10	9	10	9	10
Basic earnings per common share ($)	**0.38**	0.34	0.35	0.28	0.31	0.32	0.35	0.36

1 *Effective 1 January 2018 the bank adopted IFRS 9 on a retrospective basis without restatement of prior periods. Results from prior periods are reported in accordance with IAS 39.*

Comments on trends over the past eight quarters

Seasonal factors did not have a significant impact on our results.

Net interest income remained relatively stable throughout 2016 and early 2017. Beginning the third quarter of 2017 it started to trend upwards as a result of growth in loans and advances and the impact of increased interest rates.

Net fee income showed strong growth during the second and third quarters of 2018, primarily as a result of higher credit facility fees as lending volumes grew, offset partly by higher fee expenses. This follows a decline in fee income during the previous two quarters as underwriting fee income declined while credit card reward incentives paid to new customers and brokerage expenses increased.

Due to the nature of net income from financial instruments held for trading, it can fluctuate from quarter to quarter. The first two quarters of 2018 increased as a result of higher derivative sales and the impact of higher gross contractual interest rates on trading instruments. The third quarter saw a slight decline due to hedge ineffectiveness leading to a loss in the current quarter and lower net interest income from debt securities due to fluctuations in yield and lower average trading balances.

Other items of income has increased on a year-to date basis due to higher gains the on sale of financial investments arising from the continued re-balancing of the bank's liquid assets, and higher income from Group entities for information technology services performed by the bank. The timing of the disposal of securities and the recharges to Group led to the variances between the quarters.

Strong credit performance led to a net recovery position on the change in expected credit losses[1] for most periods since the fourth quarter of 2016, although this has reduced from the high recovery levels experienced in 2017. The fourth quarter of 2017 saw an increase in specific loan impairment charges in Commercial Banking, leading to a net charge for that period. Effective 1 January 2018 the bank adopted IFRS 9. Recoveries in the first half of 2018 relate to improvements in several sectors, most notably the energy services and manufacturing sector, together with allowance reversals relating to certain energy services, manufacturing, construction, and real estate companies.

On a year-to-date basis there has been a small increase in operating expenses. From 2015-2017 operating expenses increased as we invested in risk and compliance activities and certain restructuring and streamlining initiatives. Our focus is now on growing our business in support of our strategic plan, and operating expenses have increased to reflect this. The timing of expenses incurred led to the variances between the quarters.

1 *Effective 1 January 2018 under IFRS 9 the term 'Change in expected credit losses' is used. The equivalent term prior to 1 January 2018 under IAS 39 was 'Loan impairment charges and other credit risk provisions'.*

Management's Discussion and Analysis (continued)

Accounting matters

The bank's results are sensitive to the accounting policies that underlie the preparation of our consolidated financial statements. The bank has adopted IFRS 15 *Revenue from Contracts with Customers* and IFRS 9 *Financial Instruments* effective 1 January 2018 as disclosed in note 1 of the consolidated financial statements.

A summary of our other significant accounting policies are provided in note 2 of our Annual Report and Accounts 2017.

Transition to IFRS 9 - Effect on business model

The implementation of IFRS 9 does not result in a significant change to our business model, or that of the three HSBC global businesses that operate in Canada. This includes our strategy, product offerings and target customer segments.

Exposures in certain industry sectors, in particular those most sensitive to changes in economic conditions, were expected to be affected to a greater degree under IFRS 9. However, we have established credit risk management processes in place and we actively assess the impact of economic developments in key markets on specific customers, customer segments or portfolios. If we foresee changes in credit conditions, we will take mitigating action, including the revision of risk appetites or limits and tenors, as appropriate. In addition, we continue to evaluate the terms under which we provide credit facilities within the context of individual customer requirements, the quality of the relationship, local regulatory requirements, market practices and our local market position.

Under IFRS 9, we recognize expected credit losses on committed, undrawn exposures, including credit cards, loan commitments and financial guarantees. We continue to manage undrawn exposures and credit limits as part of our overall approach to capital management.

Critical accounting estimates and judgments

The preparation of financial information requires the use of estimates and judgments about future conditions and are contained in the 'Critical accounting estimates and judgments' section of the Management's Discussion and Analysis of our Annual Report and Accounts 2017, except those noted below relating to expected credit losses (which replaces 'impairment of loans and advances') resulting from the adoption of the new IFRS standards as disclosed in note 1 of the consolidated financial statements.

Business model assessment

A business model refers to the actual management of financial assets in order to generate cash flows and create value and whether likely inflows will result primarily from the collection of contractual cash flows, sales proceeds or both. It reflects the strategic purpose and intention for the portfolio and how its performance is measured by the bank. This assessment of the business model primarily takes place when a financial asset is initially recognized and is a matter of fact, not an accounting policy choice.

Expected credit losses

The recognition and measurement of expected credit losses ('ECL') is highly complex and involves the use of significant judgment and estimation, including in the formulation and incorporation of multiple forward-looking economic conditions into the ECL estimates to meet the measurement objectives of IFRS 9.

In determining ECL, management is required to exercise judgment in defining what is considered to be a significant increase in credit risk and in making assumptions and estimates to incorporate relevant information about past events, current conditions and forecasts of economic conditions. Further information about the key judgments involved is included in note 1 under sections 'Significant increase in credit risk (stage 2)' and 'Forward-looking economic inputs'. In addition, as set out in the section 'Period over which ECL is measured' of note 1, judgment has been applied in determining the lifetime and point of initial recognition of revolving facilities.

The Probability of Default ('PD'), Loss Given Default ('LGD') and Exposure at Default ('EAD') models which support these determinations are reviewed regularly in light of differences between loss estimates and actual loss experience.

Management exercises judgment in making estimations that require the use of assumptions which are highly subjective and very sensitive to the risk factors, in particular to changes in economic and credit conditions. Many of the factors have a high degree of interdependency and there is no single factor to which loan impairment allowances as a whole are sensitive.

Economic and market review and outlook[1]

After posting a six year rate of growth of 3%, the fastest among G7 nations in 2017, we expect the Canadian economy to expand at a more moderate pace in coming years. HSBC Bank Canada expects Gross Domestic Product ('GDP') growth to slow to 2% in 2018, and to 1.7%, in both 2019 and 2020.

Drivers

We believe that the main reason driving the slowdown in GDP is our expectation of a slower growth in consumption resulting in a smaller positive contribution to growth in GDP. We expect consumption's growth contribution to drop by 40% to 1.2 percentage points in 2018, down from 2.0 percentage points in 2017. There are two factors causing the slowdown in consumption growth: first, consistent with slower economic growth, we predict employment growth to decline. After growing by 1.9% in 2017, we predict employment growth to slow to 1.2% in 2018, before slowing to 0.8% in 2019. Second, we expect the pace of consumer household borrowing to slow in response to rising interest rates and the tighter mortgage lending standards introduced in January 2018.

Meanwhile, though we anticipate growth in exports and business investment to increase at a faster pace compared to recent years, we expect these gains to be moderate and not sufficient enough to offset the impact of a slower growth in consumption as noted above. We forecast exports to grow by 2.9% in 2018, which is up from 1.1% in 2017. However, in Q2 2018 exports were boosted by temporary gains

Management's Discussion and Analysis (continued)

in a few sectors, including rebounds in aluminum and steel following earlier declines owing to US tariffs. We predict export growth to dip to 2.7% in 2019 and to 2.4% in 2020. We base our positive outlook for exports on improvements in indicators of global demand and on currency weakness. That said, we expect lingering competitive challenges to limit export growth.

Additionally, we forecast business investment to rise by 6.3% in 2018, the quickest increase in six years. However, this is largely due to an increase in imports of heavy machinery expected prior to a change in Federal environmental regulations. As a result, there is limited evidence that business investment is rising due to firms bumping up against capacity constraints. In 2019 and 2020, we expect business investment to grow to 2.5% and 3.1%.

USMCA

There has been some better news on business investment heading into 2019 as a result of the result of the US, Mexico, and Canada agreeing on a new trilateral trade agreement, the United States-Mexico-Canada Agreement ('USMCA'), which is set to replace the North American Free Trade Agreement (NAFTA). While this will remove a headwind that had been holding back non-energy business investment, we still see a moderate profile for overall business investment in coming years owing to stagnating oil sector investment. While some global oil prices are nearing multi-year highs, a key Canadian oil price remains near three-year lows. As a result, the gap between global oil price benchmarks and Canadian oil has hit a record high. Along with uncertainty over additional pipeline capacity, oil sector investment remains muted.

Inflation

We predict inflation to rise to 2.3% in 2018, up from 1.6% in 2017. The increase in inflation is seen as partly driven by temporary factors. As well, inflation has been boosted by a change in the way airfares prices are tracked that resulted in a record 16.4% increase in airfares in July 2018. We see limited evidence that the increase in inflation is the result of excess demand, or an economy that is operating at potential. With a forecast of moderate economic growth, we anticipate underlying inflation to remain around the Bank of Canada's 2% inflation target in coming years.

The Bank of Canada's Governing Council has indicated that higher rates will be warranted, but that it plans to raise rates in a gradual manner. However, with our modest growth and inflation forecasts, and concerns about the possible impact of higher interest rates on heavily indebted households we expect a very shallow trajectory for Bank of Canada rate hikes. The neutral rate is expected to be between 2.5% and 3.5%, which is 100 basis points above the current policy rate. Short-term interest rates are priced for between three and four rate hikes by the end of 2019. We consider this too aggressive given the overhang of household and non-financial corporate debt, and look for at most, two rate hikes.

Trade

On the fiscal front, while trade policy progress has been made, assuming USMCA is successfully approved in the US and Mexico, the competitive challenges that have weighed on exports remain. Competitive pressures were exacerbated by reductions to US corporate taxes, and we await a Federal response to help level the playing field.

That said, Canada is well positioned to take advantage of trade agreements that will result in increased access to Europe, and Asia, in addition to the US. First, the USMCA removes a source of trade policy uncertainty. Second, the free trade deal with the European Union (the Comprehensive Economic and Trade Agreement, CETA) came into force, on a provisional basis in late 2017. Third, Canada has also signed free trade deal with several Asian Nations (the Comprehensive and Progressive Agreement for Trans-Pacific Partnership, CPTPP), that, when ratified, will lower barriers to trade with Australia, Brunei, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, Vietnam. There is thus great scope for trade to support growth in coming years, and a strong incentive for Canadian firms to overcome competitive headwinds.

1 *The predictions and forecasts in this section are based on information and assumptions from sources we consider reliable. If this information or these assumptions are not accurate, actual economic outcomes may differ materially from the outlook presented in this section.*

Regulatory developments

Basel Committee

In December 2017, the Basel Committee ('Basel') published revisions to the Basel III framework. The final package includes:

- widespread changes to the risk weights under the Standardized approach to credit risk;
- a change in the scope of application of the internal ratings based ('IRB') approach to credit risk, together with changes to the IRB methodology;
- the replacement of the operational risk approaches with a single methodology;
- an amended set of rules for the credit valuation adjustment capital framework;
- an aggregate output capital floor that ensures that banks' total risk-weighted assets are no lower than 72.5% of those generated by the revised Standardized approach; and
- changes to the exposure measure for the leverage ratio.

Basel has announced that the package will be implemented on 1 January 2022, with a five-year transitional provision for the output floor from that date.

Canada

In January 2018, OSFI announced its decision to update the existing capital floor for institutions using advanced approaches for credit risk and operational risk. Effective from the second quarter of 2018, the capital floor was based on the Standardized approach under Basel II framework with the floor factor transitioned in over three quarters. The floor factor was set at 70% for the second quarter of 2018, increasing to 72.5% in the third quarter of 2018 and 75% in the fourth quarter of 2018. This interim step will improve the risk-sensitivity

Management's Discussion and Analysis (continued)

of the capital floor while ensuring the objectives of the floor continue to be met until the proposed implementation of the Basel III capital floor begins in 2022.

OSFI reiterated its support for implementing the Basel III reforms published by the Basel in December 2017. In July 2018 OSFI has proposed to make certain modifications to the reforms for implementation in Canada to accommodate the unique characteristics of the Canadian market.

Off-balance sheet arrangements

As part of our banking operations, we enter into a number of off-balance sheet financial transactions that have a financial impact, but may not be recognized in our consolidated financial statements. These types of arrangements are contingent and may not necessarily, but in certain circumstances could, involve us incurring a liability in excess of amounts recorded in our consolidated balance sheet. These arrangements include: guarantees and letters of credit and are described in the 'Off-balance sheet arrangements' section of our Annual Report and Accounts 2017.

Related party transactions

We enter into transactions with other HSBC affiliates as part of the normal course of business, such as banking and operational services. In particular, as a member of one of the world's largest financial services organizations, we share in the expertise and economies of scale provided by the HSBC Group. We provide and receive services or enter into transactions with a number of HSBC Group companies, including sharing in the cost of development for technology platforms used around the world and benefit from worldwide contracts for advertising, marketing research, training and other operational areas. These related party transactions are on terms similar to those offered to non-related parties and are subject to formal approval procedures that have been approved by the bank's Conduct Review Committee. For further information refer to note 30 of our Annual Report and Accounts 2017.

As a wholly-owned subsidiary, all of our common shares and preferred shares are indirectly held by HSBC Holdings.

Disclosure controls and procedures and internal control over financial reporting

The Chief Executive Officer and Chief Financial Officer have signed certifications relating to the appropriateness of the financial disclosures in interim filings with the Canadian Securities Administrators, including this MD&A and the accompanying consolidated financial statements for the quarter ended 30 September 2018, and their responsibility for the design and maintenance of disclosure controls and procedures and internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting in accordance with IFRSs. There have been no changes in internal controls over financial reporting during the quarter ended 30 September 2018 that have materially affected or are reasonably likely to affect internal control over financial reporting. On 1 January 2018, HSBC Bank Canada adopted IFRS 9. Relevant internal controls over financial reporting have been updated and modified as a result of the new accounting standard.

Risk management

Refer to the "Risk management" section of our Annual Report and Accounts 2017 for a description of how the bank manages risk on an enterprise wide level, as well as the management of reputation and operational risk.

Credit risk

Credit risk is the risk of financial loss if a customer or counterparty fails to meet an obligation under contract. It arises principally from direct lending, trade finance and the leasing business, but also from other products such as guarantees and credit derivatives and from holding assets in the form of debt securities.

The bank's principal objectives of credit risk management are:

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

Refer to the 'Risk management' section of our Annual Report and Accounts 2017 for a discussion of how the bank manages credit risk, collateral and other credit risk enhancements, as well as a more in depth explanation of our credit risk measures.

Adoption of IFRS 9

Effective 1 January 2018, the bank adopted IFRS 9 which introduces ECL and replaces the incurred loss model under IAS 39.

The impairment requirements apply to financial assets measured at amortized cost and fair value through other comprehensive income ('FVOCI'), lease receivables and certain loan commitments and financial guarantee contracts.

At initial recognition, an impairment allowance is required for ECL resulting from default events that are possible within the next 12 months ('12-month ECL'). In the event of a significant increase in credit risk, an allowance is required for ECL resulting from all possible default events over the expected life of the financial instrument ('lifetime ECL'). Financial assets where 12-month ECL is recognized are considered to be 'stage 1'; financial assets that are considered to have experienced a significant increase in credit risk are in 'stage 2'; and financial assets for which there is objective evidence of impairment are considered to be in default or otherwise credit impaired are in 'stage 3'.

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

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

If such unlikeliness to pay is not identified at an earlier stage, it is deemed to occur when an exposure is 90 days past due. Therefore, the definitions of credit-impaired and default are aligned as far as possible so that stage 3 represents all loans which are considered defaulted or otherwise credit-impaired. Interest income on stage 3 exposures is recognized by applying the effective interest rate to the amortized cost amount, i.e. gross carrying amount less ECL allowance.

The assessment of credit risk and the estimation of ECL are required to be unbiased and probability-weighted, and to incorporate all available information relevant to the assessment, including information about past events, current conditions and reasonable and supportable forecasts of economic conditions at the reporting date. In addition, the estimation of ECL takes into account the time value of money. As a result, the recognition and measurement of impairment is more forward-looking than under IAS 39 and the resulting impairment charge will tend to be more volatile.

More information on IFRS 9 and ECL can be found in note 1 and note 7 of the consolidated financial statements.

Credit risk profile

The following tables and analysis provide information on financial instruments to which the impairment requirements of IFRS 9 are applied. In addition to the analysis below, further information on the credit quality of our portfolio is available in note 7 of the consolidated financial statements.

Allowance for expected credit losses (balance sheet)

	30 Sep 2018	1 Jan 2018[1]
	$m	$m
Retail:		
Performing loans (stage 1 and 2)	**31**	31
Non-performing loans (stage 3)	**18**	20
Total Retail allowance for expected credit losses	**49**	51
Wholesale:		
Performing loans (stage 1 and 2)	**101**	104
Non-performing loans (stage 3)	**116**	208
Total Wholesale allowance for expected credit losses	**217**	312
Allowance for expected credit losses	**266**	363
By global business:		
Commercial Banking	**195**	291
Global Banking and Markets	**22**	21
Retail Banking and Wealth Management	**49**	51
Allowance for expected credit losses	**266**	363

1 *The comparative period presented above represents the opening allowance for credit losses under IFRS 9, which differs from the closing allowance for impaired loans under IAS 39. Further information on the transition from IAS 39 to IFRS 9, including a reconciliation of the consolidated balance sheet as at 31 December 2017 and 1 January 2018 can be found in note 1 of the consolidated financial statements.*

The total Retail allowance for ECL decreased by $2m. This was due to a decrease in the allowance for ECL on non-performing loans as a result of write-offs and improvements in credit quality, which were partially offset by charges relating to growth in the portfolio.

The Wholesale allowance for ECL decreased by $95m, primarily due to a decrease of $92m in the non-performing portfolio. Contributing to the decrease were write-offs relating to specific customers, mainly in the manufacturing and professional, scientific and technical activities sectors. In addition, credit quality improvements across a number of sectors, most notably the energy service, manufacturing and real estate sectors, led to recoveries and transfers to the performing portfolio. These were partially offset by charges against specific clients in the construction and manufacturing industry.

Management's Discussion and Analysis (continued)

Change in expected credit losses (income statement)

The table and analysis below provides an overview of the change in expected credit losses charge or (recovery) to the income statement.

	Quarter ended	Nine months ended
	30 Sep 2018	**30 Sep 2018**
	$m	**$m**
Retail:		
Performing loans (stage 1 and 2)	**(6)**	**—**
Non-performing loans (stage 3)	**2**	**3**
Total Retail change in expected credit losses	**(4)**	**3**
Wholesale:		
Performing loans (stage 1 and 2)	**5**	**(4)**
Non-performing loans (stage 3)	**(8)**	**(45)**
Total Wholesale change in expected credit losses	**(3)**	**(49)**
Change in expected credit losses	**(7)**	**(46)**

IAS 39 comparative

	Quarter ended	Nine months ended
	30 Sep 2017	30 Sep 2017
	$m	$m
Retail:		
Collectively assessed allowances	(4)	(9)
Individually assessed allowances	2	3
Total Retail loan impairment recoveries and other credit risk provisions	(2)	(6)
Wholesale:		
Collectively assessed allowances	(10)	(27)
Individually assessed allowances	(2)	(76)
Total Wholesale loan impairment recoveries and other credit risk provisions	(12)	(103)
Total loan impairment recoveries and other credit risk provisions	(14)	(109)

The total Retail change in expected credit losses for the quarter resulted in a release of $4m. This was driven by a recovery of $6m in the performing portfolio, primarily due to the impact of updates to forward looking economic factors, in particular in the revolving credit portfolio. This was partially offset by a charge of $2m from the non-performing portfolio relating write-offs in the quarter.

For the year-to-date, the Retail change in expected credit losses resulted in a charge of $3m in the non-performing portfolio, primarily relating to write-offs.

The Wholesale change in expected credit losses for the quarter resulted in a recovery of $3m. Contributing to this were recoveries of $8m in the non-performing portfolio as a result of provision releases, primarily relating to a number of energy services and manufacturing companies. This was partially offset by charges in the non-performing portfolio against specific clients, primarily in the wholesale and retail trade industry.

The recovery in the non-performing portfolio was partially offset by a charge of $5m in the performing portfolio mainly as a result of changes in the forward looking economic factors.

For the year-to-date, the Wholesale change in expected credit losses resulted in a recovery of $49m, primarily relating to recoveries in the non-performing portfolio reflecting the continuing improvements in several sectors, most notably energy services and manufacturing together with allowance reversals mentioned above.

Impaired assets - stage 3

The following table provides an analysis of the gross carrying value of financial assets measured at amortized cost including loan commitments and financial guarantees that are determined to be impaired (stage 3 financial assets).

	30 Sep 2018	31 Dec 2017[1]
	$m	$m
Corporate and commercial[2]		
– Mining and quarrying[3]	**62**	103
– Manufacture	**32**	89
– Construction	**22**	18
– Wholesale and retail trade, repair of motor vehicles and motorcycles	**40**	41
– Transportation and storage	**7**	11
– Accommodation and food	**1**	1
– Publishing, audiovisual and broadcasting	**6**	6
– Real estate	**16**	46
– Professional, scientific and technical activities	**34**	55
– Administrative and support services	**1**	—
Total corporate and commercial	**221**	370
Financial institutions	**2**	6
Households[4]	**70**	78
Total on-balance sheet exposures	**293**	454
Off-balance sheet exposures	**89**	131
Total impaired financial assets	**382**	585

1 *Effective 1 January 2018 the bank adopted IFRS 9 on a retrospective basis without restatement of prior periods. Results from prior periods are reported in accordance with IAS 39.*

2 *The corporate and commercial categories reported above are derived from Nomenclature des Activités Économiques dans la Communauté Européenne ('NACE') codes- a European industry standard classification system. These are not directly comparable to the industry sectors previously disclosed under IAS 39.*

3 *Mining and quarrying includes energy related exposures.*

4 *Households includes the Retail portfolio.*

Impaired assets decreased from $585m as at 31 December 2017 to $382m as at 30 September 2018. This was primarily as a result of improvements in several sectors, most notably manufacturing, mining and quarrying (which includes energy related exposures), professional, scientific and technical activities, and real estate.

Impaired assets were comprised of $258m loans and advances to customers, $35m other financial assets, $56m loans and other credit related commitments and $33m financial guarantees and similar commitments.

Days past due but not impaired loans and advances

The aging analysis below includes past due loans on which stage 1 and stage 2 allowances have been assessed but do not meet the requirements to be determined credit impaired and in stage 3.

	30 Sep 2018	31 Dec 2017
	$m	$m
Up to 29 days	**1,443**	1,577
30-59 days	**13**	125
60-89 days	**55**	63
	1,511	1,765

Mortgages and home equity lines of credit

The bank's mortgage and home equity lines of credit portfolios are considered to be low-risk since the majority are secured by a first charge against the underlying real estate. The tables below detail how the bank mitigates risk further by diversifying the geographical markets in which it operates as well as benefiting from borrower default insurance. In addition, the bank maintains strong underwriting and portfolio monitoring standards to ensure the quality of its portfolio is maintained.

Management's Discussion and Analysis (continued)

Insurance and geographic distribution[1]	Residential mortgages					HELOC[2]	
	Insured[3]		Uninsured		Total	Uninsured	
30 September 2018:	**\$m**	**%**	**\$m**	**%**	**\$m**	**\$m**	**%**
British Columbia	**975**	**7**	**13,051**	**93**	**14,026**	**870**	**100**
Western Canada[4]	**349**	**25**	**1,044**	**75**	**1,393**	**592**	**100**
Ontario	**944**	**11**	**7,279**	**89**	**8,223**	**94**	**100**
Quebec and Atlantic provinces	**248**	**21**	**926**	**79**	**1,174**	**212**	**100**
Total	**2,516**	**10**	**22,300**	**90**	**24,816**	**1,768**	**100**
31 December 2017:							
British Columbia	759	6	12,850	94	13,609	867	100
Western Canada4	289	22	1,040	78	1,329	220	100
Ontario	747	10	6,573	90	7,320	591	100
Quebec and Atlantic provinces	207	18	951	82	1,158	94	100
Total	2,002	9	21,414	91	23,416	1,772	100

1 *Geographic location is determined by the address of the originating branch.*

2 *HELOC is an abbreviation for Home Equity Lines of Credit, which are lines of credit secured by equity in real estate.*

3 *Insured mortgages are protected from potential losses caused by borrower default through the purchase of insurance coverage, either from the Canadian Housing and Mortgage Corporation or other accredited private insurers.*

4 *Western Canada excludes British Columbia.*

Amortization period[1]	Residential mortgages			
	Less than 20 years	**20 - 24 years**	**25- 29 years**	**30 - 34 years**
Total at 30 September 2018	**20.2%**	**38.9%**	**40.8%**	**0.0%**
Total at 31 December 2017	20.8 %	33.0 %	45.9 %	0.2 %

1 *Amortization period is based on the remaining term of residential mortgages.*

Average loan-to-value ratios of new originations[1, 2,3]

	Uninsured % LTV[4]	
	Residential mortgages	**HELOC**
	%	%
British Columbia	**54.1%**	**49.4%**
Western Canada[5]	**67.0%**	**66.6%**
Ontario	**60.7%**	**55.6%**
Quebec and Atlantic provinces	**62.4%**	**57.3%**
Total Canada for the quarter ended 30 September 2018	**59.1%**	**54.2%**
Total Canada for the quarter ended 31 December 2017	60.1 %	54.7 %

1 *All new loans and home equity lines of credit were originated by the bank; there were no acquisitions during the period.*

2 *New originations excludes existing mortgage renewals.*

3 *Where a HELOC is advanced with a mortgage on the same property, loan-to-value is comprised of both.*

4 *Loan-to-value ratios are simple averages, based on property values at the date of mortgage origination.*

5 *Western Canada excludes British Columbia.*

Potential impact of an economic downturn on residential mortgage loans and home equity lines of credit

The bank performs stress testing on its Retail portfolio to assess the impact of increased levels of unemployment, rising interest rates, reduction in property values and changes in other relevant macroeconomic variables. Potential increase in losses in the mortgage portfolio under downturn economic scenarios are considered manageable given the diversified composition of the portfolio, the low Loan to Value in the portfolio and risk mitigation strategies in place.

Liquidity and funding risk

Liquidity risk is the risk that the bank does not have sufficient financial resources to meet its obligations as they fall due, or will have to do so at an excessive cost. This risk arises from mismatches in the timing of cash flows.

Funding risk is the risk that funding considered to be sustainable, and therefore used to fund assets, is not sustainable over time. The risk arises when the funding needed for illiquid asset positions cannot be obtained at the expected terms and when required.

Liquidity and funding risk management

Our liquidity and funding management strategy as described in the 'Liquidity and funding risk' section of our Annual Report and Accounts 2017 continues to apply. The bank's internal liquidity and funding risk management framework uses the liquidity coverage ratio ('LCR') and net stable funding ratio ('NSFR') regulatory framework as a foundation, but adds additional metrics, limits and overlays to address the risks that the bank considers are not adequately reflected by the external regulatory framework.

We continue to monitor liquidity and funding risk against our stated risk appetite and management framework.

Liquid assets

The table below shows the estimated liquidity value unweighted (before assumed haircuts) of assets categorized as liquid and used for the purpose of calculating the OSFI LCR metric. The level of liquid assets reported reflects the stock of unencumbered liquid assets at the reporting date, using the regulatory definition of liquid assets. Liquid assets consist of cash or assets that can be converted into cash at little or no loss of value.

Our liquid assets decreased by $1.3bn from 31 December 2017, primarily due to growth in loans.

Liquid assets [1]

	30 Sep 2018 $m	31 Dec 2017 $m
Level 1	**19,481**	20,307
Level 2a	**4,027**	4,491
Level 2b	**64**	119
	23,572	24,917

1 *The liquid asset balances stated here are as at the above dates (spot rate) and are unweighted and therefore do not match the liquid asset balances stated in the LCR ratio calculations which are the average for the quarter and are weighted.*

Liquidity regulation

In accordance with OSFI's Liquidity Adequacy Requirements ('LAR') guideline, which incorporates Basel liquidity standards, the bank is required to maintain a LCR above 100% as well as monitor the Net Cumulative Cash Flow ('NCCF'). The LCR estimates the adequacy of liquidity over a 30 day stress period while the NCCF calculates a horizon for net positive cash flows in order to capture the risk posed by funding mismatches between assets and liabilities. As at 30 September 2018, the bank was compliant with both requirements.

As a basis to determine the bank's stable funding requirement, the bank calculates the NSFR according to Basel Committee on Banking Supervision ('BCBS') publication number 295, pending its implementation in Canada and Europe expected in 2020 and 2021 respectively. The NSFR requires banks to maintain a stable funding profile relative to the composition of their assets and off-balance sheet activities and reflects a bank's long-term funding profile (funding with a term of more than a year). It is designed to complement the LCR.

The bank's OSFI LCR is summarized in the following table. For the quarter ended 30 September 2018, the bank's average LCR of 135% is calculated as the ratio of High-Quality Liquid Assets (HQLA) to the total net stressed cash outflows over the next 30 calendar days. HQLA is substantially comprised of Level 1 assets such as cash, deposits with central banks and highly rated securities issued or guaranteed by governments, central banks and supranational entities. The average LCR increased this quarter over the average for the previous quarter mainly due to an increase in HQLA, primarily as a result of increased long and short-term funding.

OSFI liquidity coverage ratio[1]

	Average for the three months ended[1]	
	30 Sep 2018	30 Jun 2018
Total HQLA[2] ($m)	**23,158**	21,672
Total net cash outflows[2] ($m)	**17,159**	16,748
Liquidity coverage ratio (%)	**135**	130

1 *The data in this table has been calculated using averages of the three month-end figures in the quarter. Consequently, the LCR is an average ratio for the three months of the quarter and might not equal the LCR ratios calculated dividing total weighted HQLA by total weighted net cash outflows.*

2 *These are weighted values and are calculated after the application of the weights prescribed under the OSFI LAR Guideline for HQLA and cash inflows and outflows.*

Management's Discussion and Analysis (continued)

Market risk

Market risk is the risk that movements in market risk factors, including interest rates, foreign exchange rates, credit spreads, commodity prices and equity prices, which will adversely affect our income or the value of our assets and liabilities.

Market risk management is independent of the business and is responsible for establishing the policies, procedures and limits that are aligned with the risk appetite of the bank. The objective of market risk management is to identify, measure and control market risk exposures in order to optimize return on risk and to remain within the bank's risk appetite.

Refer to the 'Risk management' section of our Annual Report and Accounts 2017 for a discussion of how the bank manages market risk as well as a more in depth explanation of our market risk measures.

Value at Risk ('VaR')

VaR is a technique that estimates the potential losses that could occur on risk positions as a result of movements in market rates and prices over a specified time horizon at a given level of confidence.

VaR disclosed in the table and graph below is the bank's total VaR for both trading and non-trading books which remained within the bank's limits during the quarter.

Total VaR decreased from September 2017 to September 2018 mainly due to a decrease in interest rate risk in the non-trading activities. This was primarily due to improved granularity in the VaR calculation with regards to exposures to Canadian government agencies during the reporting period. Over the same period, the average non-trading VaR decreased by $20.2m to $10.5m.

The average trading VaR increased by $0.3m to $1.8m due to higher interest rate risk from growth in trading activities during the same period.

Total VaR

	Nine months ended	
	30 Sep 2018	30 Sep 2017
	$m	$m
At period end	**8.4**	29.4
Average	**10.8**	30.7
Minimum	**7.6**	19.7
Maximum	**16.8**	43.1

Non-trading VaR

	Nine months ended	
	30 Sep 2018	30 Sep 2017
	$m	$m
At period end	**8.4**	30.6
Average	**10.5**	30.7
Minimum	**6.7**	20.0
Maximum	**16.7**	41.5

Trading VaR (by risk type)[1]

	Foreign exchange and commodity	Interest rate	Equity	Credit Spread	Portfolio diversification[2]	Total[3]
	$m	$m	$m	$m	$m	$m
January - September 2018						
At period end	—	**1.4**	—	**0.4**	**(0.3)**	**1.5**
Average	—	**1.7**	—	**0.4**	**(0.3)**	**1.8**
Minimum[4]	—	**1.0**	—	**0.3**		**1.0**
Maximum[4]	—	**3.1**	—	**0.8**		**3.1**

	Foreign exchange and commodity	Interest rate	Equity	Credit Spread	Portfolio diversification[2]	Total[3]
	$m	$m	$m	$m	$m	$m
January - September 2017						
At period end	—	2.2	—	0.7	(0.6)	2.3
Average	—	1.3	—	0.5	(0.4)	1.5
Minimum[4]	—	0.8	—	0.2		0.9
Maximum[4]	0.1	2.5	—	1.7		2.7

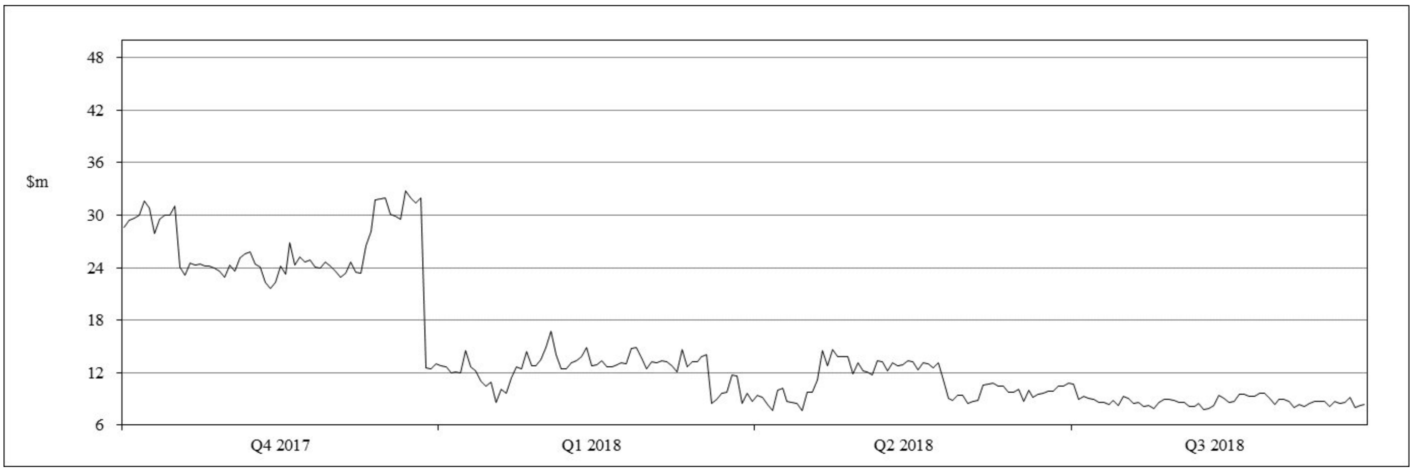
1 *Trading portfolios comprise positions arising from the market-making of financial instruments and customer-driven derivatives positions.*

2 *Portfolio diversification is the market risk dispersion effect of holding a portfolio containing different risk types. It represents the reduction in unsystematic market risk that occurs when combining a number of different risk types, for example, interest rate, equity and foreign exchange, together in one portfolio. It is measured as the difference between the combined total VaR and the sum of the VaRs by individual risk type. A negative number represents the benefit of portfolio diversification.*

3 *The total VaR is non-additive across risk types due to diversification effects.*

4 *As the maximum and minimum occur on different days for different risk types, it is not meaningful to calculate a portfolio diversification benefit for these measures. Some small differences in figures presented are due to rounding.*

Daily total VaR- 1 year history of daily figures



Structural interest rate risk

Structural interest rate risk arises primarily out of differences in the term to maturity or repricing of our assets and liabilities, both on- and off-balance sheet.

Refer to the 'Structural Interest Rate Risk' section of our Annual Report and Accounts 2017 for a discussion of how the bank manages structural interest rate risk as well as an explanation of our monitoring measures.

Sensitivity of structural interest rate risk in the non-trading portfolio

	30 Sep 2018		30 Sep 2017	
	Economic value of equity	**Earnings at risk**	Economic value of equity	Earnings at risk
	$m	**$m**	$m	$m
Before-tax impact resulting from an immediate and sustained shift in interest rates				
100 basis point increase	**(253)**	**101**	(264)	93
100 basis point decrease	**218**	**(84)**	209	(109)

Factors that may affect future results

The risk management section in the MD&A describes the most significant risks to which the bank is exposed and, if not managed appropriately, could have a material impact on our future financial results.

Refer to the 'Factors that may affect future results' section of our Annual Report and Accounts 2017 for a description of additional factors which may affect future financial results.

Management's Discussion and Analysis (continued)

Capital

Our objective in the management of capital is to maintain appropriate levels of capital to support our business strategy and meet our regulatory requirements.

Refer to the 'Capital' section of our Annual Report and Accounts 2017 for a discussion of how the bank manages its capital.

Regulatory capital and capital ratios in the tables below are presented under a Basel III 'all-in' basis, under which non-qualifying capital instruments are phased out over 10 years starting 1 January 2013.

The bank remained within its required regulatory capital limits during the quarter ended 30 September 2018.

Regulatory capital ratios

Actual regulatory capital ratios and capital requirements

	30 Sep 2018	31 Dec 2017
Actual regulatory capital ratios[1]	**%**	%
Common equity tier 1 capital ratio	**11.1**	10.5
Tier 1 capital ratio	**13.3**	12.4
Total capital ratio	**15.9**	14.7
Leverage ratio	**4.5**	4.9
Regulatory capital requirements[2]		
Minimum common equity tier 1 capital ratio	**7.0**	7.0
Minimum tier 1 capital ratio	**8.5**	8.5
Minimum total capital ratio	**10.5**	10.5

1 *Presented under a Basel III "all-in" basis with non-qualifying capital instruments phased out over 10 years starting 1 January 2013.*

2 *OSFI target capital ratios on an 'all-in' basis including mandated capital conservation buffer.*

Regulatory capital

Regulatory capital and risk-weighted assets

	30 Sep 2018	31 Dec 2017
	$m	$m
Tier 1 capital	**5,259**	5,589
Common equity tier 1 capital	**4,409**	4,739
Gross common equity[1]	**4,576**	4,860
Regulatory adjustments	**(167)**	(121)
Additional tier 1 eligible capital	**850**	850
Tier 2 capital[2]	**1,043**	1,042
Total capital	**6,302**	6,631
Risk-weighted assets (RWA) used in the calculation[3,4]		
Common equity tier 1 capital RWA	**39,584**	45,035
Tier 1 capital RWA	**39,601**	45,035
Total capital RWA	**39,618**	45,035

1 *Includes common share capital, retained earnings and accumulated other comprehensive income.*

2 *Includes capital instruments subject to phase out and allowances.*

3 *Each capital ratio has its own RWA measure due to the OSFI-prescribed scalar for inclusion of the Credit Valuation Adjustment (CVA). For fiscal 2018, the scalars for inclusion of CVA for Common equity tier 1, Tier 1, and Total capital RWA are 80%, 83%, and 86%. For fiscal 2017, the scalars were 72%, 77%, and 81%.*

4 *In January 2018, OSFI announced its decision to update the existing capital floor for institutions using advanced approaches for credit risk and operational risk. Effective from the second quarter of 2018, the capital floor was based on the Standardized approach under Basel II framework with the floor factor transitioned in over three quarters. The floor factor was set at 70% for the second quarter of 2018, increasing to 72.5% in the third quarter of 2018 and 75% in the fourth quarter of 2018.*

Outstanding shares and dividends

	30 Sep 2018			31 Dec 2017		
	Cumulative dividend	**Number of issued shares**	**Carrying value**	Dividend	Number of issued shares	Carrying value
	$ per share	**000's**	**$m**	$ per share	000's	$m
Common shares	**1.48395**	**498,668**	**1,225**	0.47126	498,668	1,225
Class 1 preferred shares[1]						
Series C[2]	**—**	**—**	**—**	1.27500	—	—
Series D[2]	**—**	**—**	**—**	1.25000	—	—
Series G	**0.75000**	**20,000**	**500**	1.00000	20,000	500
Series I[3]	**0.94500**	**14,000**	**350**	0.00000	14,000	350

1 *Cash dividends on preferred shares are non-cumulative and are payable quarterly.*

2 *Preferred shares – Class 1, Series C and D were redeemed on 31 December 2017.*

3 *Preferred shares – Class 1 Series I were issued on 7 December 2017; initial dividends were declared during the first quarter of 2018 and paid in accordance with their terms in the usual manner on 31 March 2018 or the first business day thereafter.*

During the third quarter of 2018, the bank declared $70m in dividends on HSBC Bank Canada common shares (paid within the quarter) and $9m in dividends on all series of HSBC Bank Canada Class 1 preferred shares (paid in accordance with their terms in the usual manner on 30 September 2018 or the first business day thereafter).

On 26 October 2018, the bank declared regular quarterly dividends for the fourth quarter 2018 on all series of HSBC Bank Canada Class 1 preferred shares, to be paid in accordance with their terms in the usual manner on 31 December 2018 or the first business day thereafter to shareholders of record on 15 December 2018.

On 26 October 2018, the bank also declared a third interim dividend of $70m on HSBC Bank Canada common shares in respect of the financial year ending 31 December 2018, and will be paid on or before 31 December 2018 to the shareholder of record on 26 October 2018.

As the quarterly dividends on preferred shares for the fourth quarter 2018 and the third interim dividend on common shares for 2018 were declared after 30 September 2018, the amounts have not been included in the balance sheet of the bank as a liability.

Interim Condensed Consolidated Financial Statements (unaudited)

Consolidated Financial Statements and Notes on the Financial Statements

Consolidated income statement (unaudited)

		Quarter ended		Nine months ended	
		30 Sep 2018[1]	30 Sep 2017	**30 Sep 2018[1]**	30 Sep 2017
	Notes	**$m**	$m	**$m**	$m
Interest income		**631**	481	**1,747**	1,384
Interest expense		**(299)**	(189)	**(790)**	(525)
Net interest income		**332**	292	**957**	859
Fee income		**195**	187	**573**	547
Fee expense		**(20)**	(18)	**(64)**	(53)
Net fee income		**175**	169	**509**	494
Net income from financial instruments held for trading (2017: Net trading income)		**35**	41	**110**	94
Changes in fair value of long-term debt (2017: Net expense from financial instruments designated at fair value)		**—**	—	**—**	(4)
Gains less losses from financial investments		**18**	4	**45**	25
Dividend income		**1**	—	**1**	—
Other operating income		**27**	22	**77**	62
Total operating income		**588**	528	**1,699**	1,530
Change in expected credit losses	7	**7**	n/a	**46**	n/a
Loan impairment recoveries and other credit risk provisions		**n/a**	14	**n/a**	109
Net operating income		**595**	542	**1,745**	1,639
Employee compensation and benefits	2	**(179)**	(183)	**(539)**	(537)
General and administrative expenses		**(131)**	(134)	**(401)**	(388)
Depreciation of property, plant and equipment		**(8)**	(7)	**(24)**	(23)
Amortization of intangible assets		**(6)**	(3)	**(12)**	(8)
Total operating expenses		**(324)**	(327)	**(976)**	(956)
Operating profit		**271**	215	**769**	683
Share of profit in associates		**—**	3	**—**	6
Profit before income tax expense		**271**	218	**769**	689
Income tax expense		**(73)**	(56)	**(208)**	(173)
Profit for the period		**198**	162	**561**	516
Profit attributable to the common shareholder		**189**	153	**533**	488
Profit attributable to preferred shareholders		**9**	9	**28**	28
Profit attributable to shareholders		**198**	162	**561**	516
Average number of common shares outstanding (000's)		**498,668**	498,668	**498,668**	498,668
Basic and diluted earnings per common share ($)		**$ 0.38**	$ 0.31	**$ 1.07**	$ 0.98

1 *Effective 1 January 2018 the bank adopted IFRS 9* Financial instruments *('IFRS 9') on a retrospective basis without restatement of prior periods. Results from prior periods are reported in accordance with IAS 39* Financial Instruments: Recognition and Measurement *('IAS 39').*

The accompanying notes and 'Risk management' and 'Capital' sections within the Management's Discussion and Analysis form an integral part of these consolidated financial statements.

Consolidated statement of comprehensive income (unaudited)

	Quarter ended		Nine months ended	
	30 Sep 2018	30 Sep 2017	**30 Sep 2018**	30 Sep 2017
	$m	$m	**$m**	$m
Profit for the period	**198**	162	**561**	516
Other comprehensive income/(loss)				
Items that will be reclassified subsequently to profit or loss when specific conditions are met:				
Debt instruments at fair value through other comprehensive income	**(39)**	n/a	**(94)**	n/a
– fair value losses	**(35)**	n/a	**(83)**	n/a
– fair value gains transferred to income statement on disposal	**(18)**	n/a	**(45)**	n/a
– income taxes	**14**	n/a	**34**	n/a
Available-for-sale investments	**n/a**	(15)	**n/a**	5
– fair value (losses)/gains	**n/a**	(16)	**n/a**	32
– fair value gains transferred to income statement on disposal	**n/a**	(4)	**n/a**	(25)
– income taxes	**n/a**	5	**n/a**	(2)
Cash flow hedges	**(19)**	(55)	**(23)**	(97)
– fair value gains/(losses)	**69**	31	**(33)**	33
– fair value (gains)/losses transferred to income statement	**(95)**	(105)	**1**	(164)
– income taxes	**7**	19	**9**	34
Items that will not be reclassified subsequently to profit or loss:				
Remeasurement of defined benefit plans	**9**	11	**31**	(10)
– before income taxes	**12**	15	**42**	(14)
– income taxes	**(3)**	(4)	**(11)**	4
Changes in fair value of financial liabilities designated at fair value due to movement in own credit risk	**—**	—	**—**	3
– before income taxes	**—**	—	**—**	3
– income taxes	**—**	—	**—**	—
Equity instruments designated at fair value through other comprehensive income	**(1)**	n/a	**(1)**	n/a
– fair value losses	**(1)**	n/a	**(1)**	n/a
– income taxes	**—**	n/a	**—**	n/a
Other comprehensive loss for the period, net of tax	**(50)**	(59)	**(87)**	(99)
Total comprehensive income for the period attributable to shareholders	**148**	103	**474**	417

The accompanying notes and 'Risk management' and 'Capital' sections within the Management's Discussion and Analysis form an integral part of these consolidated financial statements.

Consolidated balance sheet (unaudited)

	Notes	30 Sep 2018[1] $m	31 Dec 2017 $m
ASSETS			
Cash and balances at central bank		**69**	411
Items in the course of collection from other banks		**37**	25
Trading assets	4	**4,008**	5,373
Other financial assets mandatorily measured at fair value through profit or loss		**5**	—
Derivatives	5	**3,413**	3,675
Loans and advances to banks		**1,348**	1,221
Loans and advances to customers	7	**54,114**	50,337
Reverse repurchase agreements – non-trading		**7,765**	6,153
Financial investments	8	**23,978**	22,913
Other assets	6	**2,654**	899
Prepayments and accrued income		**308**	213
Customers' liability under acceptances		**5,627**	4,801
Current tax assets		**48**	44
Property, plant and equipment		**92**	106
Goodwill and intangible assets		**112**	90
Deferred taxes		**99**	118
Total assets		**103,677**	96,379
LIABILITIES AND EQUITY			
Liabilities			
Deposits by banks		**1,110**	1,696
Customer accounts		**57,982**	57,054
Repurchase agreements – non-trading		**8,793**	4,604
Items in the course of transmission to other banks		**227**	299
Trading liabilities	9	**1,634**	3,701
Derivatives	5	**3,202**	3,516
Debt securities in issue	10	**13,345**	10,820
Other liabilities	11	**4,462**	2,217
Acceptances		**5,635**	4,801
Accruals and deferred income		**454**	475
Retirement benefit liabilities		**303**	346
Subordinated liabilities		**1,039**	1,039
Provisions		**35**	61
Current tax liabilities		**30**	40
Total liabilities		**98,251**	90,669
Equity			
Common shares		**1,225**	1,225
Preferred shares		**850**	850
Other reserves		**(179)**	(61)
Retained earnings		**3,530**	3,696
Total equity		**5,426**	5,710
Total liabilities and equity		**103,677**	96,379

1 *Effective 1 January 2018 the bank adopted IFRS 9 on a retrospective basis without restatement of prior periods. Results from prior periods are reported in accordance with IAS 39. Refer to the table 'Reconciliation of consolidated balance sheet as at 31 December 2017 and 1 January 2018' in note 1 of the consolidated financial statements for further details of balance sheet presentation changes.*

The accompanying notes and 'Risk management' and 'Capital' sections within the Management's Discussion and Analysis form an integral part of these consolidated financial statements.

Consolidated statement of cash flows (unaudited)

		Nine months ended	
		30 Sep 2018	30 Sep 2017
	Notes	**$m**	$m
Cash flows from operating activities			
Profit before tax		**769**	689
Adjustments for:			
– non-cash items included in profit before tax	13	**13**	(57)
– change in operating assets	13	**(8,735)**	(2,296)
– change in operating liabilities	13	**10,261**	(1,591)
– tax paid		**(176)**	(116)
Net cash from operating activities		**2,132**	(3,371)
Cash flows from investing activities			
Purchase of financial investments		**(9,200)**	(5,129)
Proceeds from the sale and maturity of financial investments		**7,997**	8,280
Purchase of intangibles and property, plant and equipment		**(45)**	(38)
Proceeds from the sale of property, plant and equipment		**1**	—
Net cash from investing activities		**(1,247)**	3,113
Cash flows from financing activities			
Redemption of subordinated liabilities		**—**	(1,400)
Issuance of subordinated liabilities		**—**	1,000
Dividends paid to shareholders		**(759)**	(169)
Redemption of preferred shares		**(350)**	—
Net cash from financing activities		**(1,109)**	(569)
Net decrease in cash and cash equivalents		**(224)**	(827)
Cash and cash equivalents at the beginning of the period		**1,880**	1,650
Cash and cash equivalents at the end of the period	13	**1,656**	823
Interest			
Interest paid		**(769)**	(541)
Interest received		**1,618**	1,338

The accompanying notes and 'Risk management' and 'Capital' sections within the Management's Discussion and Analysis form an integral part of these consolidated financial statements.

Consolidated statement of changes in equity (unaudited)

	Share capital[1]	Retained earnings	Other reserves: Available-for-sale fair value reserve	Other reserves: Financial assets at FVOCI reserve	Other reserves: Cash flow hedging reserve	Other reserves: Total other reserves	Total equity
	$m	$m	$m	$m	$m	$m	$m
At 1 January 2018	**2,075**	**3,696**	**(12)**	**n/a**	**(49)**	**(61)**	**5,710**
Changes on initial application of IFRS 9	**—**	**11**	**12**	**(12)**	**—**	**—**	**11**
Restated balance at 1 January 2018 under IFRS 9	**2,075**	**3,707**	**—**	**(12)**	**(49)**	**(61)**	**5,721**
Profit for the period	**—**	**561**	**n/a**	**—**	**—**	**—**	**561**
Other comprehensive income/(loss), net of tax	**—**	**31**	**n/a**	**(95)**	**(23)**	**(118)**	**(87)**
– debt instruments at fair value through other comprehensive income	**—**	**—**	**n/a**	**(94)**	**—**	**(94)**	**(94)**
– equity instruments designated at fair value through other comprehensive income	**—**	**—**	**n/a**	**(1)**	**—**	**(1)**	**(1)**
– cash flow hedges	**—**	**—**	**n/a**	**—**	**(23)**	**(23)**	**(23)**
– remeasurement of defined benefit asset/liability	**—**	**31**	**n/a**	**—**	**—**	**—**	**31**
Total comprehensive income for the period	**—**	**592**	**n/a**	**(95)**	**(23)**	**(118)**	**474**
Dividends on common shares	**—**	**(740)**	**n/a**	**—**	**—**	**—**	**(740)**
Dividends on preferred shares	**—**	**(28)**	**n/a**	**—**	**—**	**—**	**(28)**
Shares issued under employee remuneration and share plan	**—**	**(1)**	**n/a**	**—**	**—**	**—**	**(1)**
At 30 September 2018	**2,075**	**3,530**	**n/a**	**(107)**	**(72)**	**(179)**	**5,426**

	Share capital[1]	Retained earnings	Other reserves: Available-for-sale fair value reserve	Other reserves: Cash flow hedging reserve	Other reserves: Total other reserves	Total equity
	$m	$m	$m	$m	$m	$m
At 1 January 2017	2,075	3,313	(30)	57	27	5,415
Profit for the period	—	516	—	—	—	516
Other comprehensive income/(loss), net of tax	—	(7)	5	(97)	(92)	(99)
– available-for-sale investments	—	—	5	—	5	5
– cash flow hedges	—	—	—	(97)	(97)	(97)
– remeasurement of defined benefit asset/liability	—	(10)	—	—	—	(10)
– changes in fair value of financial liabilities designated at fair value arising from changes in own credit risk	—	3	—	—	—	3
Total comprehensive income for the period	—	509	5	(97)	(92)	417
Dividends on common shares	—	(141)	—	—	—	(141)
Dividends on preferred shares	—	(28)	—	—	—	(28)
Shares issued under employee remuneration and share plan	—	(3)	—	—	—	(3)
At 30 September 2017	2,075	3,650	(25)	(40)	(65)	5,660

1 *Share capital is comprised of common shares of $1,225m and preferred shares of $850m.*

The accompanying notes and 'Risk management' and 'Capital' sections within the Management's Discussion and Analysis form an integral part of these consolidated financial statements.

Notes on the Consolidated Financial Statements (unaudited)

1 Basis of preparation and significant accounting policies

HSBC Bank Canada ('the bank', 'we', 'our') is an indirectly wholly-owned subsidiary of HSBC Holdings plc ('the Parent', 'HSBC Holdings', 'HSBC Group'). Throughout these interim condensed consolidated financial statements ('consolidated financial statements'), the 'HSBC Group' means the Parent and its subsidiary companies.

a *Compliance with International Financial Reporting Standards*

The consolidated financial statements have been prepared in accordance with International Accounting Standard ('IAS') 34 'Interim Financial Reporting' as issued by the International Accounting Standards Board ('IASB') and should be read in conjunction with the bank's 2017 audited annual consolidated financial statements. The bank's 2017 audited annual consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ('IFRSs') and accounting guidelines as issued by the Office of the Superintendent of Financial Institutions Canada ('OSFI'), as required under Section 308(4) of the Bank Act.

IFRSs comprise accounting standards as issued or adopted by the IASB and its predecessor body as well as interpretations issued or adopted by the IFRS Interpretations Committee and its predecessor body.

b *Standards adopted effective 1 January 2018*

With the exception of the provisions relating to the presentation of gains and losses on financial liabilities designated at fair value, which were adopted from 1 January 2017, the requirements of IFRS 9 *Financial Instruments* ('IFRS 9') were adopted effective 1 January 2018. IFRS 9 includes an accounting policy choice to retain the hedge accounting requirements of IAS 39 *Financial Instruments: Recognition and Measurement* ('IAS 39'), which the bank has exercised. The classification and measurement and impairment requirements are applied retrospectively by adjusting the opening balance sheet at the date of initial application, 1 January 2018, with no requirement to restate comparative periods. The bank did not restate the comparative periods. The impact of adoption on net assets at 1 January 2018 are set out on pages 41 to 42.

In addition, the bank has adopted from 1 January 2018 the requirements of IFRS 15 *Revenue from Contracts with Customers* ('IFRS 15'), which provides a principles-based approach for revenue recognition, and introduces the concept of recognizing revenue for performance obligations as they are satisfied. In accordance with IFRS 15's transition options, the bank has applied the standard retrospectively with the cumulative effect of initially applying the Standard recognized at the date of initial application as an adjustment to the opening balance of retained earnings at the date of initial application. The bank has assessed the impact of IFRS 15 and has determined that the standard has no significant effect when applied to its consolidated financial statements at the date of initial application, 1 January 2018. Therefore, no adjustment to retained earnings has been made to the consolidated financial statements.

c *Future accounting developments*

Future accounting developments have been disclosed in note 1 (c) of the 2017 annual consolidated financial statements of the bank's Annual Report and Accounts 2017, excluding the changes noted in (b) above which have been implemented effective 1 January 2018.

d *Presentation of information*

The consolidated financial statements are presented in Canadian dollars, the bank's functional currency. The abbreviation '$m' represents millions of dollars. All tabular amounts are in millions of dollars except where otherwise noted.

e *Critical accounting estimates and assumptions*

The preparation of financial information requires the use of estimates and judgments about future conditions. Management's selection of accounting policies which contain critical estimates and judgments include:

- valuation of financial instruments
- deferred tax assets
- defined benefit obligations

In view of the inherent uncertainties and the high level of subjectivity involved in the recognition or measurement of these items, it is possible that the outcomes in future reporting periods could differ from those on which management's estimates are based, resulting in materially different conclusions from those reached by management for the purposes of the consolidated financial statements. These items are described further in the 'Critical accounting estimates and judgments' section of the Management's Discussion and Analysis of the bank's Annual Report and Accounts 2017.

As a result of adopting IFRS 9 from 1 January 2018, 'impairment of loans and advances' noted in the bank's Annual Report and Accounts 2017 has been replaced with 'expected credit losses', as described in the 'Critical accounting estimates and judgments' section of the Management's Discussion and Analysis for this quarter ended 30 September 2018.

f *Consolidation*

The consolidated financial statements comprise the consolidated financial statements of the bank and its subsidiaries as at 30 September 2018. The method adopted by the bank to consolidate its subsidiaries is described in note 2 (a) of the 2017 annual consolidated financial statements of the bank's Annual Report and Accounts 2017.

g *Significant accounting policies*

Except as indicated in note (b) above, the consolidated financial statements have been prepared using the same accounting policies used in preparation of our audited 2017 annual consolidated financial statements. The bank adopted IFRS 15 on 1 January 2018 on a retrospective basis, recognizing the cumulative effect, which was nil, of initially applying the standard as an adjustment to the opening balance of retained earnings. Set out below under (h) is the accounting policy of the Bank for fee income under IFRS 15. Further, the policies under (h) have replaced the previous policy relating to "Fee income" under note 2 (b) in the bank's Annual Report and Accounts 2017.

As noted in (b) above, the bank also adopted IFRS 9 which replaces IAS 39. Set out below under (i) are the new or substantially revised accounting policies resulting from implementing IFRS 9. The accounting policies on hedge accounting are unchanged and are not repeated. Further, the policies under (i) have replaced existing policies (d), (e) and (f) in the bank's Annual Report and Accounts 2017.

h *Fee income*

Revenue is recognized when (or as) the bank satisfies a performance obligation by transferring a promised good or service (i.e. an asset) to a customer. An asset is transferred when (or as) the customer obtains control of that asset.

The recognition of revenue can be either over time or at a point in time depending on when the performance obligation is satisfied. When control of a good or service is transferred over time, if the customer simultaneously receives and consumes the benefits provided by the bank's performance as we perform, the bank satisfies the performance obligation and recognizes revenue over time. Otherwise, revenue is recognized at the point in time at which we transfer control of the good or service to the customer.

Variable consideration, where applicable, is measured using either the expected value method or the most likely amount method depending on which method the bank expects to better predict the amount of consideration to which it will be entitled. This is the estimated amount of variable consideration, or the portion, if any, of that amount for which it is highly probable that a significant reversal in the amount of cumulative revenue recognized will not occur.

For all fee types, where there is a single performance obligation, the transaction price is allocated in its entirety to that performance obligation. Where there are multiple performance obligations, the transaction price is allocated to the performance obligation to which it relates based on stand-alone selling prices.

The bank has applied the practical expedient in IFRS 15.121(a) as all of its performance obligations remaining on adoption of IFRS 15 were part of contracts that have an original expected duration of one year or less.

Income which forms an integral part of the effective interest rate of a financial instrument (for example, certain loan commitment fees) is recognized as an adjustment to the effective interest rate and recorded in 'Interest income'.

The main types of fee income arising from contracts with customers, including information about performance obligations, determining the timing and satisfaction of performance obligations and determining the transaction price and the amounts allocated to performance are as follows:

Credit facilities

Credit facility fees include fees generated from providing a credit facility that are not included within the Effective Interest Rate ('EIR'), such as annual facility fees (commitment fees), standby fees and other transaction based fees charged for late payments, return payments, over credit charges and foreign usage. Fees associated with loan commitments and standby letters of credit are billed upfront and recognized on a straight-line basis over the period the service is performed and the performance obligation is met (e.g. the commitment period). In the event a loan commitment or standby letter of credit is exercised, the remaining unamortized fee is recognized as an adjustment to yield over the loan term. The transaction price (excluding any interest element) usually includes an annual facility fee, which could be a fixed charge or a percentage of the approved credit limit, and other transaction-based charges, which could be either a fixed price or a percentage of the transaction value. Although fees charged can be variable (percentage of credit limit or transaction value), the uncertainty is resolved by the time the revenue is recognised as the credit limit or transaction value is known on the contract or transaction date. Therefore, there is no need to estimate the variable consideration or apply the constraint. On the basis that the services are provided evenly over the term of the agreement, the fee is recognized on a straight line basis over the commitment period.

Notes on the Consolidated Financial Statements (unaudited) (continued)

Funds under management

Funds under management include management fees, administration fees and transaction based fees.

Management fees are generally percentage based and therefore represent variable consideration. This amount is subject to the variable consideration constraint and is only included in the transaction price to the extent that it is highly probable that a significant reversal of cumulative revenue will not occur when the uncertainty associated with the variable consideration is subsequently resolved. At the end of each payment period, or at each reporting date, the management fee is allocated to the distinct management services that have been provided during that period. Fee income from management fees is recognized evenly over time on a straight-line basis as the services are provided and the related performance obligations are satisfied evenly over time. The fee percentage and payment period are agreed with the customer upfront. Generally, payment periods are monthly or quarterly and coincide with our reporting periods, thereby resolving the uncertainty of the variable consideration by the reporting date. For payment periods that do not coincide with our reporting periods, judgment is required to estimate the fee and determine the amount to recognize as accrued income, accrued income is only recorded to the extent it is highly probably that a significant reversal of revenue will not occur. A significant reversal of accrued management fee revenue is not highly probable for most contracts.

Administration fees, where applicable, are agreed with the customer and based on the terms of each contract. These fees are either fixed upfront charges or percentage based fees calculated as a percentage of the average value of a customer's assets at the end of an agreed period. Percentage based administrative fees are included in the transaction price only to the extent that it is highly probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty associated with the variable consideration is resolved.

Other fees are transaction based and are recognized and billed at the point in time the transaction occurs and the performance obligation is met.

Cards

Credit card arrangements involve numerous contracts between various parties. The bank has determined that the more significant contracts within the scope of IFRS 15 are:

- the contract between the bank and the credit card holder ('Cardholder Agreement') under which we earn miscellaneous fees (e.g., late payment fees, over-limit fees, foreign exchange fees, etc.) and for some products annual fees; and
- an implied contract between the bank and merchants who accept our credit cards in connection with the purchase of their goods and/or services ('Merchant Agreement') under which we earn interchange fees.

The Cardholder Agreement obligates the bank, as the card issuer, to perform activities such as redeem loyalty points by providing goods, cash or services to the cardholder, provide ancillary services such as concierge services, travel insurance, airport lounge access and the like, process late payments, provide foreign exchange services, and others. The primary fees arising under cardholder agreements which are in scope of IFRS 15 include annual fees, transaction based fees, and penalty fees for late payments. The amount of each fee stated in the contract represents the transaction price for that performance obligation. Annual fees on credit cards are billed upfront and recognized on a straight-line basis. Other credit card fees, as noted above, are transaction based and are recognized and billed at the point in time the transaction occurs and the performance obligation is met.

Interchange fees

The implied contract between the bank and the merchant results in the bank receiving an interchange fee from the merchant. The interchange fee represents the transaction price associated with the implied contract between the bank and the merchant because it represents the amount of consideration to which the bank expects to be entitled in exchange for transferring the promised service (i.e., purchase approval and payment remittance) to the merchant. The performance obligation associated with the implied contract between the bank and the merchant is satisfied upon performance and simultaneous consumption by the customer of the underlying service (i.e. purchase approval and payment remittance). Therefore, the interchange fee is recognized as revenue each time the bank approves a purchase and remits payment to the merchant.

Account services

The bank provides services for current accounts that generate fees from various activities including: accounts statements, ATM transactions, cash withdrawals, wire transfers, utilization of cheques, debit cards and internet and phone banking. The fees for these services are established in the customer account agreement and are either billed individually at the time the service is performed and the performance obligation is met, or on a monthly basis for a package or bundle of services as the services are performed and the performance obligation is met. Customer account agreements typically include a package of services with multiple performance obligations or a bundle of services making up a single performance obligation. In the case of a package of services, the pattern of transfer to the customer is the same for all services (stand ready obligation) therefore, all the goods and services are treated as a single performance obligation. The transaction price is allocated in its entirety to the single performance obligation. The performance obligation associated with account services is satisfied as a stand ready obligation to provide services evenly over time, and therefore, the fee income from account services is recognized evenly over time.

i *Accounting policies resulting from implementing IFRS 9*

Classification and Measurement of Financial Assets

The Bank classifies its financial instruments under IFRS 9 into the following categories:

i) Financial instruments measured at amortized cost;

ii) Financial assets measured at fair value through other comprehensive income ('FVOCI');

iii) Equity securities measured at fair value with fair value movements presented in other comprehensive income ('OCI'); and

iv) Financial instruments designated and otherwise mandatorily measured at fair value through profit or loss.

(i) Financial instruments measured at amortized cost

Financial assets that are held to collect the contractual cash flows and that contain contractual terms that give rise on specified dates to cash flows that are solely payments of principal and interest, such as most loans and advances to banks and customers and some debt securities, are measured at amortized cost and are presented net of an allowance for expected credit losses. In addition, most financial liabilities are measured at amortized cost. The carrying value of these financial assets at initial recognition includes any directly attributable transaction costs. If the initial fair value is lower than the cash amount advanced, such as in the case of some leveraged finance and syndicated lending activities, the difference is deferred and recognized over the life of the loan through the recognition of interest income, unless the loan becomes impaired. The bank may commit to underwriting loans on fixed contractual terms for specified periods of time. When the loan arising from the lending commitment is expected to be held for trading, the commitment to lend is recorded as a derivative. When the bank intends to hold the loan, the loan commitment is included in the impairment calculations set out below.

(ii) Financial assets measured at FVOCI

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

(iii) Equity securities measured at fair value with fair value movements presented in OCI

The equity securities for which fair value movements are shown in OCI are business facilitation and other similar investments. Gains or losses on the derecognition of these equity securities are not transferred to profit or loss. Otherwise equity securities are measured at fair value through profit or loss (except for dividend income which is recognized in profit or loss).

(iv) Financial instruments designated and otherwise mandatorily measured at fair value through profit or loss

Equity securities for which the fair value movements are not shown in OCI are mandatorily classified in this category.

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

– the use of the designation removes or significantly reduces an accounting mismatch;

– when a group of financial assets and liabilities or a group of financial liabilities is managed and its performance is evaluated on a fair value basis, in accordance with a documented risk management or investment strategy; and

– where the financial liability contains one or more non-closely related embedded derivatives.

Designated financial assets are recognized when the bank enters into contracts with counterparties, which is generally on trade date, and are normally derecognized when the rights to the cash flows expire or are transferred. Designated financial liabilities are recognized when the bank enters into contracts with counterparties, which is generally on settlement date, and are normally derecognized when extinguished. Subsequent changes in fair values are recognized in the income statement in 'Changes in fair value of long-term debt'.

Under the above criterion, there are no such financial instruments designated at fair value by the bank at 30 September 2018.

Notes on the Consolidated Financial Statements (unaudited) (continued)

Derivatives

Derivatives are financial instruments that derive their value from the price of underlying items such as equities, interest rates or other indices. Derivatives are recognized initially and are subsequently measured at fair value. Derivatives are classified as assets when their fair value is positive or as liabilities when their fair value is negative. This includes embedded derivatives in financial liabilities which are bifurcated from the host contract when they meet the definition of a derivative on a stand-alone basis when the entire contract, including the host instrument, is not designated at fair value through profit or loss.

Where the derivatives are managed with debt securities issued by the bank that are designated at fair value, the contractual interest is shown in 'Interest expense' together with the interest payable on the issued debt.

Impairment of amortized cost and FVOCI financial assets

Expected credit losses ('ECL') are recognized for loans and advances to banks and customers, non-trading reverse repurchase agreements, other financial assets held at amortized cost, debt instruments measured at fair value through other comprehensive income, and certain loan commitments and financial guarantee contracts. At the end of the first reporting period after initial recognition, an allowance (or provision in the case of some loan commitments and financial guarantees) is required for ECL resulting from default events that are possible within the next 12 months (or less, where the remaining life is less than 12 months) ('12-month ECL'). In the event of a significant increase in credit risk, an allowance (or provision) is required for ECL resulting from all possible default events over the expected life of the financial instrument ('lifetime ECL'). Financial assets where 12-month ECL is recognized are considered to be 'stage 1'; financial assets which are considered to have experienced a significant increase in credit risk are in 'stage 2'; financial assets for which there is objective evidence of impairment so are considered to be in default or otherwise credit-impaired are in 'stage 3'.

Credit-impaired (stage 3)

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

– contractual payments of either principal or interest are past due for more than 90 days;

– there are other indications that the borrower is unlikely to pay such as that a concession has been granted to the borrower for economic or legal reasons relating to the borrower's financial condition; and

– the loan is otherwise considered to be in default.

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

Write-off

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

Renegotiation

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

A loan that is renegotiated is derecognized if the existing agreement is canceled and a new agreement is made on substantially different terms or if the terms of an existing agreement are modified such that the renegotiated loan is a substantially different financial instrument. Any new loans that arise following derecognition events in these circumstances are considered to be purchased or originated credit-impaired financial assets ('POCI') and will continue to be disclosed as renegotiated loans.

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

Loan modifications that are not credit-impaired

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

Significant increase in credit risk (stage 2)

An assessment of whether credit risk has increased significantly since initial recognition is performed at each reporting period by considering the change in the risk of default occurring over the remaining life of the financial instrument. The assessment explicitly or implicitly compares the risk of default occurring at the reporting date compared to that at initial recognition, taking into account reasonable and supportable information, including information about past events, current conditions and future economic conditions. The assessment is unbiased, probability-weighted, and to the extent relevant, uses forward-looking information consistent with that used in the measurement of ECL. The analysis of credit risk is multi-factor.

The determination of whether a specific factor is relevant and its weight compared with other factors depends on the type of product, the characteristics of the financial instrument and the borrower, and the geographical region. Therefore, it is not possible to provide a single set of criteria that will determine what is considered to be a significant increase in credit risk and these criteria will differ for different types of lending, particularly between retail and wholesale. However, unless identified at an earlier stage, all financial assets are deemed to have suffered a significant increase in credit risk when payments are 30 days past due. In addition, wholesale loans that are individually assessed, typically corporate and commercial customers, and included on a watch or worry list are included in stage 2.

For wholesale portfolios, the quantitative comparison assesses default risk using a lifetime probability of default which encompasses a wide range of information including the obligor's customer risk rating, macroeconomic condition forecasts and credit transition probabilities. Significant increase in credit risk is measured by comparing the average PD for the remaining term estimated at origination with the equivalent estimation at reporting date. The significance of changes in PD was informed by expert credit risk judgment, referenced to historical credit migrations and to relative changes in external market rates.

For loans originated prior to the implementation of IFRS 9, the origination PD does not include adjustments to reflect expectations of future macroeconomic conditions since these are not available without the use of hindsight. In the absence of this data, the origination PD is approximated assuming through-the-cycle ('TTC') PDs and TTC migration probabilities, consistent with the instrument's underlying modeling approach and the credit risk rating ('CRR') at origination.

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

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

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

ECL resulting from default events that are possible within the next 12 months ('12-month ECL') are recognized for financial instruments that remain in stage 1.

Movement between stages

Financial assets can be transferred between the different categories depending on their relative increase or decrease in credit risk since initial recognition. Financial instruments are transferred out of stage 2 if their credit risk is no longer considered to be significantly increased since initial recognition based on the assessments described above. Except for renegotiated loans, financial instruments are transferred out of stage 3 when they no longer exhibit any evidence of credit impairment as described above. Renegotiated loans will continue to be in stage 3 until there is sufficient evidence to demonstrate a significant reduction in the risk of non-payment of future cash flows, observed over a minimum one-year period and there are no other indicators of impairment. For loans that are assessed for impairment on a portfolio basis, the evidence typically comprises a history of payment performance against the original or revised terms,

Notes on the Consolidated Financial Statements (unaudited) (continued)

as appropriate to the circumstances. For loans that are assessed for impairment on an individual basis, all available evidence is assessed on a case-by-case basis.

Measurement of ECL

The assessment of credit risk, and the estimation of ECL, are unbiased and probability-weighted, and incorporate all available information which is relevant to the assessment including information about past events, current conditions and reasonable and supportable forecasts of future events and economic conditions at the reporting date. In addition, the estimation of ECL should take into account the time value of money. In general, the bank calculates ECL using three main components, a probability of default, a loss given default and the exposure at default ('EAD').

The 12-month ECL is calculated by multiplying the 12-month PD, LGD and EAD. Lifetime ECL is calculated using the lifetime PD instead. The 12-month and lifetime PDs represent the probability of default occurring over the next 12 months and the remaining maturity of the instrument respectively. The EAD represents the expected balance at default, taking into account the repayment of principal and interest from the balance sheet date to the default event together with any expected drawdowns of committed facilities. The LGD represents expected losses on the EAD given the event of default, taking into account, among other attributes, the mitigating effect of collateral value at the time it is expected to be realized and the time value of money. The bank leverages the Basel II IRB framework where possible, with recalibration to meet the differing IFRS 9 requirements as follows:

Model	Regulatory capital	IFRS 9
PD	– Through the cycle (represents long-run average PD through a full economic cycle) – The definition of default includes a backstop of 90+ days past due	– Point in time (based on current conditions, adjusted to take into account estimates of future conditions that will impact PD) – Default backstop of 90+ days past due
EAD	– Cannot be lower than current balance	– Amortization captured for term products
LGD	– Downturn LGD (consistent losses expected to be suffered during a severe but plausible economic downturn) – Regulatory floors may apply to mitigate risk of underestimating downturn LGD due to lack of historical data – Discounted using cost of capital – All collection costs included	– Expected LGD (based on estimate of loss given default including the expected impact of future economic conditions such as the change in value of collateral – No floors – Discounted using the original effective interest rate of the loan – Only costs associated with obtaining/selling collateral included
Other		– Discounted back from point of default to balance sheet date

While 12-month PDs are recalibrated from Basel models where possible, the lifetime PDs are determined by projecting the 12-month PD using a term structure. For the wholesale methodology, the lifetime PD also takes into account credit migration, i.e. a customer migrating through the CRR bands over its life. The ECL for wholesale stage 3 is determined on an individual basis using a discounted cash flow ('DCF') methodology. The expected future cash flows are based on the credit risk officer's estimates as at the reporting date, reflecting reasonable and supportable assumptions and projections of future recoveries and expected future receipts of interest. Collateral is taken into account if it is likely that the recovery of the outstanding amount will include realization of collateral based on its estimated fair value of collateral at the time of expected realization, less costs for obtaining and selling the collateral. The cash flows are discounted at a reasonable approximation of the original effective interest rate. For significant cases, cash flows under four different scenarios are probability-weighted by reference to the three economic scenarios applied more generally by the bank and the judgment of the credit risk officer in relation to the likelihood of the workout strategy succeeding or receivership being required. For less significant cases, the effect of different economic scenarios and work-out strategies is approximated and applied as an adjustment to the most likely outcome. The movements associated with these variables are referred to as 'Changes to risk parameters (model inputs)' in note 7 'Allowance for expected credit losses'.

Period over which ECL is measured

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

Forward-looking economic inputs

The bank will in general apply three forward-looking global economic scenarios determined with reference to external forecast distributions, the Consensus Economic Scenario approach. This approach is considered sufficient to calculate unbiased expected loss in most economic environments. They represent a 'most likely outcome' (the Central scenario) and two, less likely, 'Outer' scenarios on either side of the Central, referred to as an Upside and a Downside scenario respectively. The Central scenario is used by the annual operating planning process and, with regulatory modifications, will also be used in enterprise-wide stress tests. The Upside and Downside are constructed following a standard process supported by a scenario narrative reflecting the bank's current top and emerging risks. The relationship between the Outer scenarios and Central scenario will generally be fixed with the Central scenario being assigned a weighting of 80% and the Upside and Downside scenarios 10% each, with the difference between the Central and Outer scenarios in terms of economic severity being informed by the spread of external forecast distributions among professional industry forecasts. The Outer scenarios are economically plausible, internally consistent states of the world and will not necessarily be as severe as scenarios used in stress testing.

The period of forecast is five years, after which the forecasts will revert to a view based on average past experience. The economic factors include, but are not limited to, gross domestic product, unemployment, interest rates, inflation and commercial property prices. In general, the consequences of the assessment of credit risk and the resulting ECL outputs will be probability-weighted using the standard probability weights. This probability weighting may be applied directly or the effect of the probability weighting determined on a periodic basis, at least annually, and then applied as an adjustment to the outcomes resulting from the central economic forecast. The central economic forecast is updated quarterly. The bank recognizes that the Consensus Economic Scenario approach using three scenarios will be insufficient in certain economic environments. Additional analysis may be prepared at management's discretion, including the production of extra scenarios. If conditions warrant, this could result in a management overlay for economic uncertainty which is included in the ECL estimates.

Notes on the Consolidated Financial Statements (unaudited) (continued)

Reconciliation of consolidated balance sheet as at 31 December 2017 and 1 January 2018

					IFRS 9 reclassification to					
	IAS 39 measurement category	**IFRS 9 measurement category**	**IAS 39 carrying amount as at 31 Dec 2017**	**Other changes in classification[1]**	**Fair value through profit and loss**	**Fair value through other comprehensive income**	**Amortized cost**	**Carrying amount post reclassification**	**IFRS 9 remeasurement including ECL**	**IFRS 9 carrying amount at 1 Jan 2018**
Assets										
Cash and balances at central bank	Amortized cost	Amortized cost	**411**	—	—	—	—	**411**	—	**411**
Items in the course of collection from other banks	Amortized cost	Amortized cost	**25**	—	—	—	—	**25**	—	**25**
Trading assets	FVPL	FVPL	**5,373**	**(248)**	—	—	—	**5,125**	—	**5,125**
Other financial assets mandatorily measured at FVPL	FVPL	FVPL	—	—	**9**	—	—	**9**	—	**9**
Derivatives	FVPL	FVPL	**3,675**	—	—	—	—	**3,675**	—	**3,675**
Loans and advances to banks	Amortized cost	Amortized cost	**1,221**	**(59)**	—	—	—	**1,162**	—	**1,162**
Loans and advances to customers	Amortized cost	Amortized cost	**50,337**	**(28)**	—	—	—	**50,309**	**(4)**	**50,305**
Reverse repurchase agreements - non-trading	Amortized cost	Amortized cost	**6,153**	—	—	—	—	**6,153**	—	**6,153**
Financial investments	FVOCI (Available-for-sale - debt instruments)	FVOCI	**22,884**	—	—	—	—	**22,884**	—	**22,884**
	FVOCI (Available-for-sale - equity	FVOCI	**20**	—	—	—	—	**20**	—	**20**
		FVPL	**9**	—	—	**(9)**	—	—	—	—
Other assets	Amortized cost	Amortized cost	**899**	**335**	—	—	—	**1,234**	—	**1,234**
Prepayments and accrued income	Amortized cost	Amortized cost	**213**	—	—	—	—	**213**	**12**	**225**
Customers' liability under acceptances	Amortized cost	Amortized cost	**4,801**	—	—	—	—	**4,801**	**(5)**	**4,796**
Current tax assets	n/a	n/a	**44**	—	—	—	—	**44**	—	**44**
Property, plant and equipment	n/a	n/a	**106**	—	—	—	—	**106**	—	**106**
Goodwill and intangible assets	n/a	n/a	**90**	—	—	—	—	**90**	—	**90**
Deferred taxes	n/a	n/a	**118**	—	—	—	—	**118**	**(4)**	**114**
Total assets			**96,379**	—	**9**	**(9)**	—	**96,379**	**(1)**	**96,378**

1 *Effective 1 January 2018, settlement accounts of $248m have been reclassified from 'Trading assets' to 'Other assets', and cash collateral accounts of $59m and $28m, respectively, have been reclassified from 'Loans and advances to banks' and 'Loans and advances to customers' to 'Other assets'.*

	IAS 39 measurement category	IFRS 9 measurement category	IAS 39 carrying amount as at 31 Dec 2017	Other changes in classification[1]	IFRS 9 reclassification to: Fair value through profit and loss	IFRS 9 reclassification to: Fair value through other comprehensive income	IFRS 9 reclassification to: Amortized cost	Carrying amount post reclassification	IFRS 9 remeasurement including ECL	IFRS 9 carrying amount at 1 Jan 2018
Liabilities										
Deposits by banks	Amortized cost	Amortized cost	**1,696**	**(227)**	—	—	—	**1,469**	—	**1,469**
Customer accounts	Amortized cost	Amortized cost	**57,054**	**(8)**	—	—	—	**57,046**	—	**57,046**
Repurchase agreements – non-trading	Amortized cost	Amortized cost	**4,604**	—	—	—	—	**4,604**	—	**4,604**
Items in the course of transmission to other banks	Amortized cost	Amortized cost	**299**	—	—	—	—	**299**	—	**299**
Trading liabilities	FVPL	FVPL	**3,701**	**(160)**	—	—	—	**3,541**	—	**3,541**
Derivatives	FVPL	FVPL	**3,516**	—	—	—	—	**3,516**	—	**3,516**
Debt securities in issue	Amortized cost	Amortized cost	**10,820**	—	—	—	—	**10,820**	—	**10,820**
Other liabilities	Amortized cost	Amortized cost	**2,217**	**395**	—	—	—	**2,612**	—	**2,612**
Acceptances	Amortized cost	Amortized cost	**4,801**	—	—	—	—	**4,801**	—	**4,801**
Accruals and deferred income	Amortized cost	Amortized cost	**475**	—	—	—	—	**475**	—	**475**
Retirement benefit liabilities	n/a	n/a	**346**	—	—	—	—	**346**	—	**346**
Subordinated liabilities	Amortized cost	Amortized cost	**1,039**	—	—	—	—	**1,039**	—	**1,039**
Provisions	n/a	n/a	**61**	—	—	—	—	**61**	**(12)**	**49**
Current tax liabilities	n/a	n/a	**40**	—	—	—	—	**40**	—	**40**
Total liabilities			**90,669**	—	—	—	—	**90,669**	**(12)**	**90,657**
Equity										
Common shares			**1,225**	—	—	—	—	**1,225**	—	**1,225**
Preferred shares			**850**	—	—	—	—	**850**	—	**850**
Other reserves			**(61)**	—	—	—	—	**(61)**	—	**(61)**
Retained earnings			**3,696**	—	—	—	—	**3,696**	**11**	**3,707**
Total equity			**5,710**	—	—	—	—	**5,710**	**11**	**5,721**
Total equity and liabilities			**96,379**	—	—	—	—	**96,379**	**(1)**	**96,378**

1 *Effective 1 January 2018, cash collateral accounts of $227m and $8m, respectively, have been reclassified from 'Deposits by banks' and 'Customer accounts' to 'Other liabilities', and settlement accounts of $160m have been reclassified from 'Trading liabilities' to 'Other liabilities'.*

Notes on the Consolidated Financial Statements (unaudited) (continued)

Allowance for credit losses

The following table is a comparison of impairment allowances determined in accordance with IAS 39 and IAS 37 to the corresponding impairment allowance determined in accordance with IFRS 9 as at 1 January 2018.

	IAS 39 / IAS 37 as at 31 December 2017				IFRS 9 as at 1 January 2018			
	Collectively assessed	Individually assessed	Total	Transition adjustments[1]	**Stage 1**	**Stage 2**	**Stage 3**	**Total**
	$m	$m	$m	$m	**$m**	**$m**	**$m**	**$m**
Loans at amortized cost	134	149	283	4	**30**	**77**	**180**	**287**
Customers' liability under acceptances at amortized cost	—	—	—	5	**4**	**1**	**—**	**5**
Prepayments and accrued income at amortized cost	—	—	—	41	**—**	**—**	**41**	**41**
Off-balance sheet loan commitments and financial guarantees	41	1	42	(12)	**8**	**15**	**7**	**30**
Total allowance for credit losses	175	150	325	38	**42**	**93**	**228**	**363**

1 *Included in the transition adjustments is a reclassification of $53m from interest receivable to allowance for credit losses. The impact of transition adjustments to retained earnings before tax is $15m.*

2 Employee compensation and benefits

Included within 'Employee compensation and benefits' are components of net periodic benefit cost related to the bank's pension plans and other post-employment benefits, as follows:

	Quarter ended		Nine months ended	
	30 Sep 2018	30 Sep 2017	**30 Sep 2018**	30 Sep 2017
	$m	$m	**$m**	$m
Pension plans – defined benefit	**5**	5	**14**	14
Pension plans – defined contribution	**10**	9	**31**	27
Healthcare and other post retirement benefit plans	**3**	3	**9**	10
	18	17	**54**	51

3 Segment analysis

We manage and report our operations according to four operating segments: three global businesses and a Corporate Centre. The three global businesses are Commercial Banking, Global Banking and Markets, and Retail Banking and Wealth Management. Various estimate and allocation methodologies are used in the preparation of the segment financial information. We allocate expenses directly related to earning revenue to the segment that earned the related revenue. Expenses not directly related to earning revenue, such as overhead expenses, are allocated using appropriate formulas. Segments' net interest income reflects internal funding charges and credits on the global businesses' assets, liabilities and capital at market rates, taking into account relevant terms. The offset of the net impact of these charges and credits is reflected in Corporate Centre.

	Quarter ended		Nine months ended	
	30 Sep 2018	30 Sep 2017	**30 Sep 2018**	30 Sep 2017
	$m	$m	**$m**	$m
Commercial Banking				
Net interest income	**150**	132	**434**	395
Net fee income	**79**	70	**233**	211
Net income from financial instruments held for trading (2017: Net trading income)	**9**	8	**26**	25
Gains less losses from financial investments	**—**	1	**—**	1
Dividend income	**1**	—	**1**	—
Other operating income	**3**	5	**13**	16
Total operating income	**242**	216	**707**	648
Change in expected credit losses	**3**	n/a	**50**	n/a
Loan impairment recoveries and other credit risk provisions	**n/a**	4	**n/a**	90
Net operating income	**245**	220	**757**	738
Total operating expenses	**(104)**	(98)	**(309)**	(287)
Profit before income tax expense	**141**	122	**448**	451
Global Banking and Markets				
Net interest income	**30**	28	**79**	74
Net fee income	**42**	44	**117**	118
Net income from financial instruments held for trading (2017: Net trading income)	**21**	17	**60**	35
Other operating income	**—**	—	**1**	—
Total operating income	**93**	89	**257**	227
Change in expected credit losses	**—**	n/a	**(1)**	n/a
Loan impairment recoveries and other credit risk provisions	**n/a**	8	**n/a**	13
Net operating income	**93**	97	**256**	240
Total operating expenses	**(39)**	(33)	**(116)**	(100)
Profit before income tax expense	**54**	64	**140**	140
Retail Banking and Wealth Management				
Net interest income	**129**	111	**363**	311
Net fee income	**54**	55	**159**	165
Net income from financial instruments held for trading (2017: Net trading income)	**7**	6	**21**	17
Gains less losses from financial investments	**—**	—	**—**	1
Other operating income	**3**	2	**9**	4
Total operating income	**193**	174	**552**	498
Change in expected credit losses	**4**	n/a	**(3)**	n/a
Loan impairment recoveries and other credit risk provisions	**n/a**	2	**n/a**	6
Net operating income	**197**	176	**549**	504
Total operating expenses	**(158)**	(160)	**(488)**	(453)
Profit before income tax expense	**39**	16	**61**	51

Notes on the Consolidated Financial Statements (unaudited) (continued)

	Quarter ended		Nine months ended	
	30 Sep 2018	30 Sep 2017	**30 Sep 2018**	30 Sep 2017
	$m	$m	**$m**	$m
Corporate Centre				
Net interest income	**23**	21	**81**	79
Net income from financial instruments held for trading (2017: Net trading income)	**(2)**	10	**3**	17
Changes in fair value of long-term debt (2017: Net expense from financial instruments designated at fair value)	**—**	—	**—**	(4)
Gains less losses from financial investments	**18**	3	**45**	23
Other operating income	**21**	15	**54**	42
Net operating income	**60**	49	**183**	157
Total operating expenses	**(23)**	(36)	**(63)**	(116)
Operating profit	**37**	13	**120**	41
Share of profit/(loss) in associates	**—**	3	**—**	6
Profit before income tax expense	**37**	16	**120**	47

Net fee income

	Quarter ended				
	30 Sep 2018				30 Sep 2017
	Commercial Banking	**Global Banking and Markets**	**Retail Banking and Wealth Management**	**Total**	Total
	$m	**$m**	**$m**	**$m**	$m
Account services	**10**	**1**	**3**	**14**	16
Funds under management	**—**	**—**	**49**	**49**	47
Cards	**4**	**—**	**12**	**16**	14
Credit facilities	**55**	**18**	**—**	**73**	69
Broking income	**—**	**—**	**2**	**2**	2
Imports/exports	**3**	**—**	**—**	**3**	2
Remittances	**5**	**2**	**1**	**8**	8
Underwriting	**—**	**16**	**—**	**16**	17
Insurance agency commission	**—**	**—**	**1**	**1**	2
Other	**4**	**7**	**2**	**13**	10
Fee income	**81**	**44**	**70**	**195**	187
Less: fee expense	**(2)**	**(2)**	**(16)**	**(20)**	(18)
Net fee income	**79**	**42**	**54**	**175**	169

	Nine months ended				
	30 Sep 2018				30 Sep 2017
	Commercial Banking	**Global Banking and Markets**	**Retail Banking and Wealth Management**	**Total**	Total
	$m	**$m**	**$m**	**$m**	$m
Account services	**31**	**5**	**12**	**48**	49
Funds under management	**—**	**—**	**144**	**144**	142
Cards	**13**	**—**	**32**	**45**	40
Credit facilities	**159**	**55**	**—**	**214**	201
Broking income	**—**	**—**	**7**	**7**	6
Imports/exports	**8**	**—**	**—**	**8**	7
Remittances	**16**	**6**	**3**	**25**	23
Underwriting	**1**	**39**	**—**	**40**	40
Insurance agency commission	**—**	**—**	**4**	**4**	6
Other	**15**	**17**	**6**	**38**	33
Fee income	**243**	**122**	**208**	**573**	547
Less: fee expense	**(10)**	**(5)**	**(49)**	**(64)**	(53)
Net fee income	**233**	**117**	**159**	**509**	494

Other information about the profit/(loss) for the quarter

	Commercial Banking	**Global Banking and Markets**	**Retail Banking and Wealth Management**	**Corporate Centre**	**Total**
	$m	**$m**	**$m**	**$m**	**$m**
Quarter ended 30 September 2018					
Net operating income:	**245**	**93**	**197**	**60**	**595**
External	**258**	**88**	**190**	**59**	**595**
Inter-segment	**(13)**	**5**	**7**	**1**	**—**
Quarter ended 30 September 2017					
Net operating income:	220	97	176	49	542
External	216	107	182	37	542
Inter-segment	4	(10)	(6)	12	—
Nine months ended 30 September 2018					
Net operating income:	**757**	**256**	**549**	**183**	**1,745**
External	**776**	**247**	**535**	**187**	**1,745**
Inter-segment	**(19)**	**9**	**14**	**(4)**	**—**
Nine months ended 30 September 2017					
Net operating income:	738	240	504	157	1,639
External	744	268	522	105	1,639
Inter-segment	(6)	(28)	(18)	52	—

Notes on the Consolidated Financial Statements (unaudited) (continued)

Balance sheet information

	Commercial Banking	Global Banking and Markets	Retail Banking and Wealth Management	Corporate Centre	Inter-segment	Total
	$m	$m	$m	$m	$m	$m
At 30 September 2018						
Loans and advances to customers	**22,311**	**3,696**	**28,107**	**—**	**—**	**54,114**
Customers' liability under acceptances	**4,161**	**1,452**	**14**	**—**	**—**	**5,627**
Total assets	**27,568**	**20,382**	**33,658**	**26,866**	**(4,797)**	**103,677**
Customer accounts	**19,349**	**5,709**	**30,447**	**2,477**	**—**	**57,982**
Acceptances	**4,182**	**1,453**	**—**	**—**	**—**	**5,635**
Total liabilities	**24,537**	**19,040**	**32,594**	**26,877**	**(4,797)**	**98,251**
At 31 Dec 2017						
Loans and advances to customers	19,856	3,537	26,944	—	—	50,337
Customers' liability under acceptances	3,431	1,370	—	—	—	4,801
Total assets	28,900	19,796	31,768	27,430	(11,515)	96,379
Customer accounts[1]	21,128	6,449	27,887	1,590	—	57,054
Acceptances	3,431	1,370	—	—	—	4,801
Total liabilities	25,761	18,467	30,893	27,063	(11,515)	90,669

1 *Effective 1 January 2018, $696m of Customer accounts from Commercial Banking were reclassified to Retail Banking and Wealth Management and $557m from Global Banking and Markets were reclassified to Corporate Centre to conform with changes in management reporting.*

4 Trading assets

	30 Sep 2018	31 Dec 2017
	$m	$m
Trading assets		
Not subject to repledge or resale by counterparties	**2,126**	3,424
Which may be repledged or resold by counterparties	**1,882**	1,949
	4,008	5,373
Canadian and Provincial Government bonds[1]	**2,915**	3,249
Debt securities	**331**	1,041
Total debt securities	**3,246**	4,290
Customer trading assets[2]	**—**	93
Trading assets from other banks[2]	**—**	155
Treasury and other eligible bills	**762**	835
	4,008	5,373

1 *Including government guaranteed bonds.*

2 *Settlement accounts of $248m at 31 December 2017 have been reclassified from 'Trading assets' to 'Other assets'. See notes 1 and 6 for more information.*

5 Derivatives

For a detailed description of the type and use of derivatives by the bank, please refer to the bank's accounting policies disclosed in note 2 of the bank's Annual Report and Accounts 2017.

Fair values of derivatives by product contract type held

	30 Sep 2018					
	Assets			**Liabilities**		
	Trading	**Hedging**	**Total**	**Trading**	**Hedging**	**Total**
	$m	**$m**	**$m**	**$m**	**$m**	**$m**
Foreign exchange	**1,276**	**53**	**1,329**	**1,246**	**70**	**1,316**
Interest rate	**1,822**	**232**	**2,054**	**1,742**	**114**	**1,856**
Commodity	**30**	**—**	**30**	**30**	**—**	**30**
Equity	**—**	**—**	**—**	**—**	**—**	**—**
Gross total fair values	**3,128**	**285**	**3,413**	**3,018**	**184**	**3,202**

	31 Dec 2017					
	Assets			Liabilities		
	Trading	Hedging	Total	Trading	Hedging	Total
	$m	$m	$m	$m	$m	$m
Foreign exchange	1,445	76	1,521	1,390	70	1,460
Interest rate	1,987	148	2,135	1,936	103	2,039
Commodity	17	—	17	17	—	17
Equity	2	—	2	—	—	—
Gross total fair values	3,451	224	3,675	3,343	173	3,516

Trading derivatives

Notional contract amounts of derivatives held for trading purposes by product type

	30 Sep 2018	31 Dec 2017
	$m	$m
Foreign exchange	**116,836**	108,943
Interest rate	**251,509**	282,198
Commodity	**104**	226
Equity	**—**	7
	368,449	391,374

The notional or contractual amounts of these instruments indicate the nominal value of transactions outstanding at the reporting date; they do not represent amounts at risk.

Hedging instruments

Notional contract amounts of derivatives held for hedging purposes by product type

	30 Sep 2018		31 Dec 2017	
	Cash flow hedge	**Fair value hedge**	Cash flow hedge	Fair value hedge
	$m	**$m**	$m	$m
Foreign exchange	**2,030**	**—**	2,398	—
Interest rate	**6,647**	**12,294**	4,697	12,056

Notes on the Consolidated Financial Statements (unaudited) (continued)

Fair value of derivatives designated as fair value hedges

	30 Sep 2018		31 Dec 2017	
	Assets	**Liabilities**	Assets	Liabilities
	$m	**$m**	$m	$m
Interest rate	**232**	**15**	146	31

Gains or losses arising from the change in fair value of fair value hedges

	Quarter ended		Nine months ended	
	30 Sep 2018	30 Sep 2017	**30 Sep 2018**	30 Sep 2017
	$m	$m	**$m**	$m
Gains/(losses):				
– on hedging instruments	**80**	82	**182**	117
– on hedged items attributable to the hedged risk	**(80)**	(79)	**(180)**	(116)

The gains and losses on ineffective portions of fair value hedges are recognized immediately in 'Net income from financial instruments held for trading'.

Fair value of derivatives designated as cash flow hedges

	30 Sep 2018		31 Dec 2017	
	Assets	**Liabilities**	Assets	Liabilities
	$m	**$m**	$m	$m
Foreign exchange	**53**	**70**	77	70
Interest rate	**—**	**99**	2	72

Gains or losses arising from the change in fair value of cash flow hedges

The gains and losses on ineffective portions of cash flow hedges are recognized immediately in 'Net income from financial instruments held for trading'. The change in fair value of cash flow hedges due to hedge ineffectiveness for the quarter ended 30 September 2018 and nine months ended 30 September 2018 was a loss of $1m (2017: loss for the quarter ended 30 September was $1m and loss for the nine months ended 30 September was $2m).

6 Other assets

	30 Sep 2018	31 Dec 2017
	$m	$m
Accounts receivable and other	**931**	774
Investments in associates	**40**	40
Due from clients, dealers and clearing corporations	**98**	73
Settlement accounts[1]	**1,360**	—
Cash collateral[2]	**217**	—
Other non-financial assets	**8**	12
	2,654	899

1 *Settlement accounts of $248m at 31 December 2017 were reclassified from 'Trading assets' to 'Other assets' as of 1 January 2018.*

2 *Cash collateral accounts at 31 December 2017 of $59m and $28m, respectively, were reclassified from 'Loans and advances to banks' and 'Loans and advances to customers' to 'Other assets' as of 1 January 2018.*

7 Allowance for expected credit losses

Financial assets classified at amortized cost are presented on the consolidated balance sheet net of the allowance for expected credit losses.

Allowance for expected credit losses

Reconciliation of allowances/provision for financial assets measured at amortized cost, including loan commitments and financial guarantees, as at and for the quarter and nine months ended 30 September 2018

	Quarter ended				Nine months ended			
	Non credit impaired		Credit impaired		Non credit impaired		Credit impaired	
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
	$m	$m	$m	$m	$m	$m	$m	$m
Balance at the beginning of the period	**35**	**99**	**150**	**284**	**42**	**93**	**228**	**363**
Transfers of financial instruments:								
– transfers from stage 1 to stage 2	**(4)**	**4**	**—**	**—**	**(12)**	**12**	**—**	**—**
– transfers from stage 2 to stage 1	**7**	**(7)**	**—**	**—**	**28**	**(28)**	**—**	**—**
– transfers to stage 3	**(1)**	**(2)**	**3**	**—**	**(2)**	**(5)**	**7**	**—**
– transfers from stage 3	**—**	**2**	**(2)**	**—**	**2**	**18**	**(20)**	**—**
– net remeasurement of ECL arising from transfer of stage	**(5)**	**4**	**—**	**(1)**	**(20)**	**12**	**—**	**(8)**
Changes due to modifications not derecognized	**—**	**—**	**—**	**—**	**—**	**—**	**—**	**—**
New financial assets originated or purchased	**10**	**—**	**—**	**10**	**33**	**3**	**—**	**36**
Changes to risk parameters (model inputs)	**5**	**1**	**(2)**	**4**	**(9)**	**7**	**(9)**	**(11)**
Assets derecognized (including final repayments)	**(5)**	**(10)**	**—**	**(15)**	**(20)**	**(23)**	**(11)**	**(54)**
Assets written off	**—**	**—**	**(15)**	**(15)**	**—**	**—**	**(61)**	**(61)**
Foreign exchange	**—**	**(1)**	**—**	**(1)**	**—**	**1**	**—**	**1**
Others	**—**	**—**	**—**	**—**	**—**	**—**	**—**	**—**
At 30 September 2018	**42**	**90**	**134**	**266**	**42**	**90**	**134**	**266**
ECL income statement (release)/charge for the period	**7**	**(8)**	**(1)**	**(2)**	**—**	**(4)**	**(33)**	**(37)**
Add: Recoveries	**—**	**—**	**(4)**	**(4)**	**—**	**—**	**(8)**	**(8)**
Add: Others	**—**	**—**	**(1)**	**(1)**	**—**	**—**	**(1)**	**(1)**
Total ECL income statement (release)/ charge for the period	**7**	**(8)**	**(6)**	**(7)**	**—**	**(4)**	**(42)**	**(46)**

Notes on the Consolidated Financial Statements (unaudited) (continued)

	Quarter ended				Nine months ended			
	Non credit impaired		Credit impaired		Non credit impaired		Credit impaired	
	Stage 1	Stage 2	Stage 3	Total	Stage 1	Stage 2	Stage 3	Total
	$m	$m	$m	$m	$m	$m	$m	$m
Wholesale portfolio								
Balance at the beginning of the period	**24**	**73**	**133**	**230**	**33**	**71**	**208**	**312**
Transfers of financial instruments:								
– transfers from stage 1 to stage 2	(4)	4	—	—	(11)	11	—	—
– transfers from stage 2 to stage 1	3	(3)	—	—	15	(15)	—	—
– transfers to stage 3	—	(1)	1	—	(1)	(2)	3	—
– transfers from stage 3	—	1	(1)	—	—	15	(15)	—
– net remeasurement of ECL arising from transfer of stage	(2)	2	—	—	(10)	6	—	(4)
New financial assets originated or purchased	10	—	—	10	31	3	—	34
Changes to risk parameters (model inputs)	5	3	(6)	2	(7)	—	(21)	(28)
Assets derecognized (including final repayments)	(4)	(9)	—	(13)	(18)	(21)	(11)	(50)
Assets written off	—	—	(11)	(11)	—	—	(48)	(48)
Foreign exchange	—	(1)	—	(1)	—	1	—	1
Others	—	—	—	—	—	—	—	—
At 30 September 2018	**32**	**69**	**116**	**217**	**32**	**69**	**116**	**217**
ECL income statement (release)/charge for the period	8	(3)	(6)	(1)	(1)	(3)	(44)	(48)
Add: Recoveries	—	—	(1)	(1)	—	—	(1)	(1)
Add: Others	—	—	(1)	(1)	—	—	—	—
Total ECL income (release)/charge for the period	8	(3)	(8)	(3)	(1)	(3)	(45)	(49)
Retail portfolio								
Balance at the beginning of the period	**11**	**26**	**17**	**54**	**9**	**22**	**20**	**51**
Transfers of financial instruments:								
– transfers from stage 1 to stage 2	—	—	—	—	(1)	1	—	—
– transfers from stage 2 to stage 1	4	(4)	—	—	13	(13)	—	—
– transfers to stage 3	(1)	(1)	2	—	(1)	(3)	4	—
– transfers from stage 3	—	1	(1)	—	2	3	(5)	—
– net remeasurement of ECL arising from transfer of stage	(3)	2	—	(1)	(10)	6	—	(4)
New financial assets originated or purchased	—	—	—	—	2	—	—	2
Changes to risk parameters (model inputs)	—	(2)	4	2	(2)	7	12	17
Assets derecognized (including final repayments)	(1)	(1)	—	(2)	(2)	(2)	—	(4)
Assets written off	—	—	(4)	(4)	—	—	(13)	(13)
At 30 September 2018	**10**	**21**	**18**	**49**	**10**	**21**	**18**	**49**
ECL income statement (release)/charge for the period	(1)	(5)	5	(1)	1	(1)	11	11
Add: Recoveries	—	—	(3)	(3)	—	—	(7)	(7)
Add: Others	—	—	—	—	—	—	(1)	(1)
Total ECL income statement (release)/charge for the period	(1)	(5)	2	(4)	1	(1)	3	3

The following table shows the continuity of our allowance for credit losses under IAS 39 for the quarter and nine months ended 30 September 2017:

Movement in impairment allowances and provision for credit losses

	Quarter ended				Nine months ended			
	Customers individually assessed	Customers collectively assessed	Other credit risk provisions	Total	Customers individually assessed	Customers collectively assessed	Other credit risk provisions	Total
	$m	$m	$m	$m	$m	$m	$m	$m
Balance at the beginning of the period	173	165	50	388	252	187	89	528
Movement								
Loans and advances written off net of recoveries of previously written off amounts[1]	(16)	—	—	(16)	(45)	(3)	(2)	(50)
Charge to income	—	(15)	1	(14)	(39)	(34)	(36)	(109)
Other movements	(4)	—	—	(4)	(15)	—	—	(15)
At 30 September 2017	153	150	51	354	153	150	51	354

1 *During the nine months ended 30 September 2017, recovered $4m of loans and advances that was written off in prior periods.*

Credit quality

Quality classification definitions

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

The five credit quality classifications defined above each encompass a range of granular internal credit rating grades assigned to wholesale and retail lending businesses and the external ratings attributed by external agencies to debt securities, as shown in the table below. Under IAS 39 retail lending credit quality was disclosed based on expected-loss percentages. Under IFRS 9 retail lending credit quality is now disclosed based on a twelve-month probability-weighted PD. The credit quality classifications for wholesale lending are unchanged and are based on internal credit risk ratings.

Quality classification

	Debt securities and other bills	**Wholesale lending**		**Retail lending**	
	External credit rating	**Internal credit rating**	**12-month Basel probability of default %**	**Internal credit rating**	**12-month Basel probability-weighted PD %**
Strong	A– and above	CRR1 to CRR2	0.000-0.169	Band 1 and 2	0.000-0.500
Good	BBB+ to BBB-	CCR3	0.170-0.740	Band 3	0.501-1.500
Satisfactory	BB+ to B and unrated	CCR4 to CCR5	0.741-4.914	Band 4 and 5	1.501-20.000
Sub-standard	B- to C	CRR6 to CRR8	4.915-99.999	Band 6	20.001-99.999
Impaired	Default	CRR9 to CRR10	100.000	Band 7	100.000

Notes on the Consolidated Financial Statements (unaudited) (continued)

The following table shows the distribution of financial instruments to which the impairment requirements in IFRS 9 are applied, by credit quality and stage allocation.

	Gross carrying/notional amount							
	Strong	Good	Satisfactory	Sub-standard	Credit impaired	Total	Allowance for ECL	Net
	$m	$m	$m	$m	$m	$m	$m	$m
Debt instruments at fair value through other comprehensive income[1]	23,969	—	—	—	—	23,969	—	23,969
– stage 1	23,969	—	—	—	—	23,969	—	23,969
– stage 2	—	—	—	—	—	—	—	—
– stage 3	—	—	—	—	—	—	—	—
Loans and advances to customers at amortized cost	25,302	16,343	11,144	1,262	258	54,309	(195)	54,114
– stage 1	25,286	16,020	8,978	182	—	50,466	(31)	50,435
– stage 2	16	323	2,166	1,080	—	3,585	(68)	3,517
– stage 3	—	—	—	—	258	258	(96)	162
Loans and advances to banks at amortized cost	1,348	—	—	—	—	1,348	—	1,348
– stage 1	1,348	—	—	—	—	1,348	—	1,348
– stage 2	—	—	—	—	—	—	—	—
– stage 3	—	—	—	—	—	—	—	—
Other financial assets at amortized cost	9,719	3,674	2,827	125	35	16,380	(42)	16,338
– stage 1	9,719	3,652	2,585	35	—	15,991	(4)	15,987
– stage 2	—	22	242	90	—	354	(4)	350
– stage 3	—	—	—	—	35	35	(34)	1
Loan and other credit-related commitments	12,932	19,456	8,360	1,149	56	41,953	(23)	41,930
– stage 1	12,854	19,114	7,191	99	—	39,258	(6)	39,252
– stage 2	78	342	1,169	1,050	—	2,639	(15)	2,624
– stage 3	—	—	—	—	56	56	(2)	54
Financial guarantees and similar commitments	2,379	2,162	738	213	33	5,525	(6)	5,519
– stage 1	2,379	2,162	616	13	—	5,170	(1)	5,169
– stage 2	—	—	122	200	—	322	(3)	319
– stage 3	—	—	—	—	33	33	(2)	31
At 30 September 2018	75,649	41,635	23,069	2,749	382	143,484	(266)	143,218

1 *The allowance for expected credit losses for debt instruments at fair value through other comprehensive income is presented in other reserves, as the related securities are recorded at fair value on the balance sheet.*

In assessing and monitoring for credit risk concentration under IAS 39, exposures were measured at exposure at default ('EAD'), which reflects drawn balances as well as an allowance for undrawn amounts of commitments and contingent exposures.

	31 December 2017		
	EAD Drawn	EAD Undrawn	EAD Total
	$m	$m	$m
Credit quality of wholesale portfolio			
Strong	29,961	3,066	33,027
Good	16,922	6,398	23,320
Satisfactory	11,279	2,862	14,141
Sub-standard	1,411	608	2,019
Impaired	376	29	405
	59,949	12,963	72,912
Credit quality of retail portfolio			
Strong	13,895	1	13,896
Good	10,157	1,308	11,465
Satisfactory	1,760	332	2,092
Sub-standard	528	58	586
Impaired	82	—	82
	26,422	1,699	28,121

8 Financial investments

	30 Sep 2018	31 Dec 2017
	$m	$m
Financial investments		
Not subject to repledge or resale by counterparties	**21,936**	20,724
Which may be repledged or resold by counterparties	**2,042**	2,189
	23,978	22,913
Financial investments measured at fair value through other comprehensive income		
Canadian and Provincial Government bonds[1]	**17,543**	n/a
International Government bonds[1]	**3,019**	n/a
Other debt securities issued by banks and financial institutions	**3,118**	n/a
Treasury and eligible bills	**289**	n/a
Other securities	**9**	n/a
	23,978	n/a
Available-for-sale securities at fair value		
Canadian and Provincial Government bonds[1]	**n/a**	15,782
International Government bonds[1]	**n/a**	3,486
Other debt securities issued by banks and financial institutions	**n/a**	3,326
Treasury and eligible bills	**n/a**	290
Other securities	**n/a**	29
	n/a	22,913
	23,978	22,913

1 *Includes government guaranteed bonds.*

Notes on the Consolidated Financial Statements (unaudited) (continued)

9 Trading liabilities

	30 Sep 2018	31 Dec 2017
	$m	$m
Other liabilities – net short positions	**1,634**	3,533
Customer trading liabilities[1]	**—**	168
	1,634	3,701

1 Settlement accounts of $160m at 31 December 2017 have been reclassified from 'Trading liabilities' to 'Other liabilities'. See notes 1 and 11 for more information.

10 Debt securities in issue

	30 Sep 2018	31 Dec 2017
	$m	$m
Bonds and medium term notes	**12,481**	10,141
Money market instruments	**864**	679
	13,345	10,820

Debt securities are recorded at amortized cost.

Term to maturity		
Less than 1 year	**3,689**	1,631
1-5 years	**9,242**	7,428
5-10 years	**414**	1,761
	13,345	10,820

11 Other liabilities

	30 Sep 2018	31 Dec 2017
	$m	$m
Mortgages sold with recourse	**1,506**	1,676
Accounts payable	**235**	479
Settlement accounts[1]	**1,790**	—
Cash collateral[2]	**286**	—
Loans payable[3]	**581**	—
Other non-financial liabilities	**54**	49
Share based payment related liability	**10**	13
	4,462	2,217

1 Settlement accounts of $160m at 31 December 2017 were reclassified from 'Trading liabilities' to 'Other liabilities' as of 1 January 2018.

2 Cash collateral accounts at 31 December 2017 of $227m and $8m, respectively, were reclassified from 'Deposits by banks' and 'Customer accounts' to 'Other liabilities' as of 1 January 2018.

3 During the third quarter, the bank entered into two USD borrowing agreements with the HSBC Group.

12 Fair values of financial instruments

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal, or in its absence, the most advantageous market to which the bank has access to at that date. The fair value of a liability reflects its non-performance risk.

Fair values are determined according to the following hierarchy:

(a) *Level 1 – quoted market price:* financial instruments with quoted prices for identical instruments in active markets.

(b) *Level 2 – valuation technique using observable inputs*: financial instruments with quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in inactive markets and financial instruments valued using models where all significant inputs are observable.

(c) *Level 3 – valuation technique with significant unobservable inputs:* financial instruments valued using models where one or more significant inputs are unobservable.

The best evidence of fair value is a quoted price in an actively traded market. In the event that the market for a financial instrument is not active, a range of valuation techniques is used, dependent on the instrument type and available market data. Most valuation techniques are based upon discounted cash flow analyses using observable market data, including prices available from exchanges, dealers, brokers or providers of consensus pricing. Where financial instruments are valued on the basis of valuation techniques that feature one or more significant market inputs that are unobservable, assumptions are made using estimates from historical data or other sources.

For a detailed description of fair value and the classification of financial instruments by the bank, please refer to the bank's accounting policies disclosed in note 24 of the bank's Annual Report and Accounts 2017.

The table below provides an analysis of the fair value hierarchy which has been deployed for valuing financial assets and financial liabilities measured at fair value in the consolidated financial statements.

	Valuation techniques			
	Level 1 quoted market price	**Level 2 using observable inputs**	**Level 3 with significant unobservable inputs**	**Total**
	$m	**$m**	**$m**	**$m**
At 30 September 2018				
Assets				
Trading assets	**3,923**	**85**	**—**	**4,008**
Other financial assets mandatorily measured at fair value through profit or loss	**—**	**5**	**—**	**5**
Derivatives	**—**	**3,407**	**6**	**3,413**
Financial investments: measured at fair value through other comprehensive income	**23,486**	**492**	**—**	**23,978**
Liabilities				
Trading liabilities	**1,626**	**8**	**—**	**1,634**
Derivatives	**—**	**3,196**	**6**	**3,202**
At 31 December 2017				
Assets				
Trading assets	4,695	678	—	5,373
Derivatives	—	3,674	1	3,675
Financial investments: available-for-sale	21,849	1,064	—	22,913
Liabilities				
Trading liabilities	3,503	197	1	3,701
Derivatives	—	3,515	1	3,516

Transfers between levels of the fair value hierarchy are deemed to occur at the end of each reporting period. Transfers into and out of levels of the fair value hierarchy are primarily attributable to observability of valuation inputs and price transparency.

During the quarter ended 30 September 2018, $24m of trading assets and $86m of financial investments were transferred from Level 2 to Level 1 due to increased frequency and quality of quoted prices in the active market. Also during the quarter ended 30 September 2018, $2m of trading assets and $95m of financial investments were transferred from Level 1 to Level 2 due to reduced observability of valuation inputs.

Notes on the Consolidated Financial Statements (unaudited) (continued)

Reconciliation of fair value measurements in Level 3 of the fair value hierarchy

	Assets	Liabilities	
	Derivatives	Held for trading	Derivatives
	$m	$m	$m
At 1 January 2018	**1**	**1**	**1**
Settlements	**(1)**	**(1)**	**(1)**
Purchases	**6**	**—**	**—**
New issuances	**—**	**—**	**6**
At 30 September 2018	**6**	**—**	**6**
Total gains or losses recognized in profit or loss relating to those assets and liabilities held at the end of the reporting period	**—**	**—**	**—**
At 1 January 2017	1	3	1
Settlements	(1)	(2)	(1)
Transfer in	1	—	1
At 30 September 2017	1	1	1
Total gains or losses recognized in profit or loss relating to those assets and liabilities held at the end of the reporting period	—	—	—

Fair values of financial instruments which are not carried at fair value on the balance sheet are as follows:

	30 Sep 2018		31 Dec 2017	
	Carrying amount	Fair value	Carrying amount	Fair value
	$m	$m	$m	$m
Assets				
Loans and advances to customers[1]	**54,114**	**53,889**	50,337	50,227
Liabilities				
Customer accounts	**57,982**	**58,257**	57,054	57,071
Debt securities in issue	**13,345**	**13,265**	10,820	10,836
Subordinated liabilities	**1,039**	**1,025**	1,039	1,035

1 *Loans and advances to customers specifically relating to Canada at 30 September 2018: Carrying amount $50,637m and Fair value $50,427m.*

13 Notes on the statement of cash flows

	Nine months ended	
	30 Sep 2018	30 Sep 2017
	$m	$m
Non-cash items included in profit before tax		
Depreciation and amortization	**36**	31
Share-based payment expense	**9**	7
Change in expected credit losses	**(46)**	n/a
Loan impairment recoveries and other credit risk provisions	**n/a**	(109)
Charge for defined benefit pension plans	**14**	14
	13	(57)

	Nine months ended	
	30 Sep 2018	30 Sep 2017
	$m	$m
Change in operating assets		
Change in prepayment and accrued income	**(83)**	(45)
Change in net trading securities and net derivatives	**(923)**	714
Change in loans and advances to customers	**(3,763)**	(1,751)
Change in reverse repurchase agreements - non-trading	**(1,656)**	(14)
Change in other assets	**(2,310)**	(1,200)
	(8,735)	(2,296)
Change in operating liabilities		
Change in accruals and deferred income	**(21)**	(49)
Change in deposits by banks	**(359)**	362
Change in customer accounts	**936**	(1,445)
Change in repurchase agreements – non-trading	**4,189**	(390)
Change in debt securities in issue	**2,525**	(491)
Change in financial liabilities designated at fair value	**—**	(3)
Change in other liabilities	**2,991**	425
	10,261	(1,591)

	30 Sep 2018	30 Sep 2017
	$m	$m
Cash and cash equivalents		
Cash and balances at central bank	**69**	49
Items in the course of collection from other banks, net	**(190)**	(166)
Loans and advances to banks of one month or less	**1,348**	641
Reverse repurchase agreements with banks of one month or less	**370**	235
T-Bills and certificates of deposits – three months or less	**59**	64
	1,656	823

14 Legal proceedings and regulatory matters

The bank is subject to a number of legal proceedings and regulatory matters arising in the normal course of our business. The bank does not expect the outcome of any of these proceedings, in aggregate, to have a material effect on its consolidated balance sheet or its consolidated income statement.

15 Events after the reporting period

On 19 October 2018, the bank sold its 39.5% interest in a private equity fund for $31m. The carrying value of the fund approximates its selling price.

There have been no other material events after the reporting period which would require disclosure or adjustment to the 30 September 2018 consolidated financial statements.

These consolidated financial statements were approved by the Board of Directors on 26 October 2018 and authorized for issue.

Investor Information

PRINCIPAL ADDRESSES

Vancouver:
HSBC Bank Canada
885 West Georgia Street
Vancouver, British Columbia
Canada V6C 3E9
Tel: 604-685-1000
Fax: 604-641-3098

Toronto:
HSBC Bank Canada
70 York Street
Toronto, Ontario
Canada M5J 1S9

Media Inquiries:
English: 416-868-3878 or 604-641-1905
English or French: 416-868-8282

Website
www.hsbc.ca

Social Media
Twitter: @HSBC_CA
Facebook: @HSBCCanada
YouTube: HSBC Canada

INVESTOR RELATIONS CONTACT

Enquiries may be directed to Investor Relations by writing to:

HSBC Bank Canada
Investor Relations -
Finance Department
4th Floor
2910 Virtual Way
Vancouver, British Columbia
Canada V5M 0B2
Email: investor_relations@hsbc.ca

© Copyright HSBC Bank Canada 2018

All rights reserved

No part of this publication may be reproduced, stored in a retrieval system, or transmitted, in any form or by any means, electronic, mechanical, photocopying, recording, or otherwise, without the prior written permission of HSBC Bank Canada.

Published by HSBC Bank Canada, Vancouver, BC.

Printed by RP Graphics Group Limited, Mississauga, ON

HSBC Bank Canada

885 West Georgia Street
Vancouver, British Columbia
Canada V6C 3E9
Telephone: 1 604 685 1000
www.hsbc.ca