HSBC

News Release

18 February 2020

GRUPO FINANCIERO HSBC, S.A. DE C.V.
2019 FINANCIAL RESULTS HIGHLIGHTS

- For the 12 months to 31 December 2019, Grupo Financiero's profit before tax was MXN12,021m, an increase of MXN2,273m, or 23.3%, compared with MXN9,748m for the same period of 2018.

- For the 12 months to 31 December 2019, net income was MXN8,999m, an increase of MXN1,705m, or 23.4%, compared with MXN7,294m for the same period of 2018.

- Total operating income excluding loan impairment charges was MXN48,361m, an increase of MXN5,039m or 11.6%, compared with MXN43,322m for the same period of 2018. In January 2019, HSBC launched a joint venture with Global Payments to operate its merchant acquiring services. This joint venture was completed by the sale of 50% of Global Payments Technology Mexico S.A. de C.V. and the recognition of a MXN1,296m gain on sale in total operating income.

- Loan impairment charges for the 12 months to 31 December 2019 were MXN9,149m, an increase of MXN265m, or 3.0%, compared with MXN8,884m for the same period of 2018.

- Administrative and personnel expenses for the 12 months to 31 December 2019 were MXN27,270m, an increase of MXN2,449m, or 9.9%, compared with MXN24,821m for the same period of 2018.

- The cost efficiency ratio was 56.4% for the 12 months to 31 December 2019, compared with 57.3% for the same period of 2018.

- Net loans and advances to customers were MXN387.3bn at 31 December 2019, showing an increase of MXN21.2bn, or 5.8%, compared with MXN366.1bn at 31 December 2018. Total impaired loans as a percentage of gross loans and advances at 31 December 2019 was 2.0%, in line with 1.9% reported at 31 December 2018.

- At 31 December 2019, total deposits were MXN513.5bn, an increase of MXN85.0bn, or 19.8%, compared with MXN428.5bn at 31 December 2018.

- Return on equity was 12.5% for the 12 months to 31 December 2019, whereas for the 12 months to 31 December 2018 it was 10.9%, showing an increase of 1.6% percentage points.

- At 31 December 2019, the bank's total capital adequacy ratio was 13.4% and the tier 1 capital ratio was 11.8%, compared with 12.3% and 10.4%, respectively, at 31 December 2018.

On a reported IFRS basis, for the 12 months to 31 December 2019, profit before tax was MXN13,230m, an increase of 30.3% compared to the same period in 2018. The main differences between Mexican GAAP and IFRS results for the 12 months to 31 December 2019 relate to differences in accounting for fair value adjustments on financial instruments, effective interest rate, loan impairment charges, deferred profit sharing, pensions and insurance liabilities.

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

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Significant events

In January 2020, HSBC announced the appointment of Jorge Arce as CEO of HSBC Mexico starting February 2020 replacing Nuno Matos. Following that announcement, in February 2020, HSBC informed the appointment of Nuno Matos as Chief Executive Officer of HSBC Bank Plc and Chief Executive Officer Europe effective March 2020.

In December 2019, HSBC Mexico issued an Additional Tier 1 instrument for the amount of USD 180m.

In January 2019, HSBC launched a joint venture in Mexico with Global Payments to operate its merchant acquiring services and provide best-in-class sales capabilities and bring to Mexico new card payment technologies. This joint venture was completed with the sale of 50% of Global Payments Technology Mexico S.A. de C.V. to Global Payments Acquisition Corporation 7 S.A.R.L, on 31 January 2019.

Overview

The economy remained weak in Q4 2019, which resulted in an annual contraction for the full year of 0.1%. The main driver of this performance was a fall in both industrial production and service sector activities. The main drag for growth during Q4 was construction activity, as it continued to fall at a fast pace. Inflation ended 2019 at 2.83% year on year, below market expectations and the central bank's target of 3%. Final inflation was driven by a sharp decline in the non-core component, combined with a gradual deceleration of core inflation.

Against this backdrop of weak growth and lower inflation, Mexico's central bank, Banxico, was able to cut the policy rate twice in Q4 2019. With these movements, the monetary policy rate ended 2019 at 7.25% from 7.75% in Q3 2019. In particular, the December cut from Banxico signaled a decoupling from the US monetary policy, as it was the first time in the second half of 2019 in which Banxico did not follow the Fed's movement. This meant that domestic conditions, such the widening of the negative output gap and the convergence of inflation towards the 3% target, gained relevance from the monetary policy perspective.

- For the 12 months to 31 December 2019, Grupo Financiero HSBC reported a profit before tax of MXN12,021m, an increase of MXN2,273m, or 23.3%, compared with MXN9,748m for the same period of 2018.

- Net interest income for the 12 months to 31 December 2019 was MXN33,667m, an increase of MXN2,574m, or 8.3%, compared with the same period of 2018. The increase was mainly driven by performing loans increase partially offset by an increase in funding costs.

- Loan impairment charges for the 12 months to 31 December 2019 were MXN9,149m, an increase of MXN265m, or 3.0%, compared with MXN8,884m for the same period of 2018, driven by increase in retail due to growth in the loan portfolio.

- Net fee income for the 12 months to 31 December 2019 was MXN7,738m, an increase of MXN100m, or 1.3%, compared with the same period of 2018.

- Trading income for the 12 months to 31 December 2019 was MXN4,706m, an increase of MXN1,583m, or 50.7%, compared with the same period of 2018, mainly due to an increase in banking business of MXN2,333m, partially offset by MXN732m driven by the sale of securities booked in the first quarter of 2018.

- Other operating income for the 12 months to 31 December 2019 MXN2,250m, an increase of MXN781m or 53.2% compared with the same period of 2018, mainly driven by the sale of the merchant acquiring business booked in January 2019.

- Administrative and personnel expenses for the 12 months to 31 December 2019 were MXN27,270m, an increase of MXN2,449m, or 9.9%, compared with MXN24,821m for the same period of 2018. This was mainly driven by higher staff costs across all lines of business, technology expenses and IPAB (Institute for the Protection of Bank Savings) fee costs.

- The cost efficiency ratio was 56.4% for the 12 months to 31 December 2019, compared with 57.3% for the same period of 2018.

- The effective tax rate was 25.1% for the 12 months to 31 December 2019, compared with the 25.2% for the same period of 2018.

- Net loans and advances to customers were MXN387.3bn at 31 December 2019, showing an increase in both retail and wholesale portfolios of MXN21.2bn, or 5.8%, compared with MXN366.1bn at 31 December 2018. The retail performing portfolio grew 20.0% compared with the 12 months to 31 December 2018 mainly driven by the increase in mortgage loans. The performing commercial loans, increased by 1.0%, compared with 31 December 2018. Credit cost ratio was 2.3% and loan loss reserves ratio was 3.3% at 31 December 2019.

- Total impaired loans as a percentage of gross loans and advances at 31 December 2019 was 2.0%, in line with 1.9% reported at 31 December 2018.

- Return on equity was 12.5% for the 12 months to 31 December 2019, whereas for the 12 months to 31 December 2018 it was 10.9%, showing an increase of 1.6 percentage points.

- Total loan loss allowances at 31 December 2019 were MXN13.2bn, an increase of MXN0.3bn or 2.2% compared with 31 December 2018. The total coverage ratio (allowance for loan losses divided by impaired loans) was 167.9%, at 31 December 2019 compared with 177.1% at 31 December 2018.

- At 31 December 2019, total deposits were MXN513.5bn, an increase of MXN85.0bn, or 19.8%, compared with MXN428.5bn at 31 December 2018.

- HSBC Bank Mexico profit before tax for the 12 months to 31 December 2019 was MXN9,881m, an increase of MXN2,231m or 29.2% compared with the same period of 2018.

- Net income was MXN7,374m, an increase of MXN1,538m, or 26.4% compared with the same period of 2018.

- HSBC Bank Mexico net interest income for the 12 months to 31 December 2019, was MXN31,381 an increase of MXN1,995 or 6.8%, compared with the same period of 2018.

- At 31 December 2019, the bank's total capital adequacy ratio was 13.4% and the tier 1 capital ratio was 11.8% compared with 12.3% and 10.4%, respectively, at 31 December 2018. HSBC's global strategy is to work with optimal levels of capital with a reasonable buffer above regulatory limits.

- The profit before tax of Grupo Financiero HSBC's insurance subsidiary for the 12 months to 31 December 2019 was MXN1,408m, a decrease of MXN 191m, or 11.9%, mainly driven by the non-recurrence of the gain on sale of securities booked in 2018.

HSBC Mexico S.A. (the bank) is a subsidiary of Grupo Financiero HSBC, S.A. de C.V. (Grupo Financiero HSBC) and is subject to supervision by the Mexican Banking and Securities Commission. The bank is required to file financial information on a quarterly basis (in this case for the period ended 31 December 2019) and this information is publicly available. Given that this information is available in the public domain, Grupo Financiero HSBC has elected to file this release. HSBC Seguros, S.A. de C.V. Grupo Financiero HSBC (HSBC Seguros) is Grupo Financiero HSBC's insurance subsidiary.

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

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

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

Retail Banking and Wealth Management (RBWM)

RBWM revenue for 2019 grew by 11.7%, positively impacted by MXN829m derived from the gain on sale of the merchant acquiring business reported in January 2019. Excluding this impact, revenue increased by 8.5% driven by higher lending balances as well as higher results from our Retail Business Banking proposition. End of period balances increased by 20% in lending, mainly driven by mortgages and credit cards which increased 32% and 18% respectively, gaining market share during 2019. In addition, deposits increased 5% compared to 2018.

Loan impairment charges increased by 17.8%, compared to the same period last year, aligned to the 20% lending portfolio growth.

RBWM profit before tax for the period was MXN3,386m, an increase of MXN414m, or 14%, compared with the same period last year. This was mainly due to growth in net interest income of MXN2,174m and other income of MXN754m driven by the gain on sale of the merchant acquiring business, partially offset by an increase in LIC's by MXN 1,269m and an increase in expenses of MXN1,374m.

Time deposits showed a 22% growth in revenue compared to the same period last year, driven by growth in balances of 12% mainly in the Premier proposition due to commercial activities such as special campaigns and higher average ticket accounts per capita, and higher spreads. This increase in balances, has driven upwards HSBC's market share.

Mutual funds, on the other hand, grew at double digit year on year, at a rate of 16.6%, gaining market share for the third year in a row.

HSBC Fusion, the first comprehensive service to serve business owners in Mexico, increased its SME customer base by 14.8% when compared to December 2018. The growth in balances has been significant, achieving annual growth of 10% in loans and 13% in deposits.

A year after its launch HSBC Zero & 2Now Credit Card, have been well accepted by the market. Customers using Zero card are not charged an annual fee or commission as long as they use the card at least once a month, while 2Now holders have been benefited with 2% of cash back over all purchases. During 2019, more than 480,000 HSBC Zero and 80,000 2Now cards have been sold through our digital channels, and branch network.

New Air Credit Card was launched at the end of December, designed as the lowest Interest Rate Credit Card in the market, covering a customer segment which has not been previously covered by HSBC. During its launch month 11,000 cards were ordered.

Stilo connect, first fully digital onboarding process for debit accounts, is the new personal banking proposition, offering to the customers a non presential alternative bank relationship. Since the launch more than 11,000 accounts have been opened.

Commercial Banking (CMB)

CMB revenue observed a positive trend during 2019, growing by 10.4% compared to the same period of 2018. Excluding the impact from the gain on sale of the merchant acquiring business, revenue grew 3.7%, improving net interest income by 11.3%, reflecting balance sheet expansion in both assets and liabilities. Excluding the impact of the new joint venture model for acquiring business, fees grew 3% from increased syndecated transactions and higher trade services.

Loan impairment charges reduced by 29% during 2019. The loan portfolio quality indecators remain sound.

Loan portfolio grew 9% vs prior year driven by traditional lending and significant syndecated loan transactions, mainly in large corporates and states and municipalities. Deposits grew 22% driven by customer accounts mainly in public sector.

CMB profit before tax was MXN2,653m, an increase of MXN1,054m or 66%, compared with the same period of 2018. The increase was mainly derived from growth in net interest income of MXN652m, increase in other income of MXN332m driven by the gain on sale of the merchant acquiring business, coupled with a decrease of LICs of MXN435m. Expenses growing MXN99m or 2.5%, below inflation.

Global Banking and Markets

Global Banking and Markets revenues of 2019 grew 25% compared with the same period of 2018. The increase is mainly explained by higher trading income and increase in fees from debt capital markets (DCM) and infrastructure & real estate transactions, partially offset by volume decrease in lending portfolio.

Global Banking and Markets decreased by 7.5% in its lending portfolio against 2018. This decrease was partially offset by higher deposit balances from GLCM (Global, Liquidity & Cash Management) showing a growth of 38.4% during 2019, driven primarily by higher volumes and spreads.

Loan impairment charges in 2019 were lower than the same period of 2018, reflecting significant provision releases booked during this year. The loan portfolio quality indecators remain sound.

Additionally, Global Banking and Markets maintained its strategy of reinforcing the debt and capital markets business by closing relevant transactions with local and international customers.

Global Banking and Markets profit before tax was MXN4,928m, an increase of MXN1,937m or more than 64.8%, compared with the same period of 2018, derived by growth in trading income by MXN2,013m partly offset with a decrease in net interest income by MXN1,156m and an increase in expenses by MXN42m.

During Q2, HSBC in conjunction with other financial institutions signed an agreement to extend a syndicated loan of US$8bn to Petroleos Mexicanos.

Awards

HSBC received the award for ‘Best Bank in Mexico’ granted by the British magazine *Euromoney*, due to the financial results obtained by the institution in the last year, the performance of its new products, its digital innovation and its corporate responsibility strategy focused on sustainable finance, among other aspects. The annual *Euromoney* awards recognise the performance of banks and the quality of their services, and are among the most prestigious in the financial sector.

On 10 April, during the ‘Sustainable Finance MX 19’ event in Mexico City, HSBC Mexico was recognised by the Green Finance Advisory Board and the Mexican Stock Exchange as the ‘Leading Investment Bank in the Placement of Green Bonds, Social and Sustainable Labeled in Mexico’, thereby recognising HSBC's leadership and commitment to sustainable development.

Euromoney develops a survey every year among users of solutions focused on international trade with the aim of identifying those who provide them with the best products and services, by country, region and globally. In 2019, for the second year in a row, HBSC was recognised by the British magazine *Euromoney* as the Best Bank in Mexico for Foreign Trade Solutions and as the Best Bank in Mexico for Service Quality in Foreign Trade Solutions.

Grupo Financiero HSBC’s 12 months to 2019 financial results as reported to HSBC Holdings plc, our ultimate parent company, are prepared in accordance with International Financial Reporting Standards (IFRS).

On a reported IFRS basis, for the 12 months to 31 December 2019, profit before tax was MXN13,230m, an increase of 30.3% compared to the same period in 2018. The main differences between Mexican GAAP and IFRS results for the 12 months to 31 December 2019 relate to differences in accounting for fair value adjustments on financial instruments, effective interest rate, loan impairment charges, deferred profit sharing, pensions and insurance liabilities.

About HSBC

Grupo Financiero HSBC is one of the leading financial groups in Mexico with 948 branches,595 ATMs and around 16,000 employees. For more information, visit www.hsbc.com.mx.
HSBC Holdings plc, the parent company of HSBC, is headquartered in London. HSBC serves customers worldwide from offices in 64 countries and territories in our geographical regions: Europe, Asia, North America, Latin America, and Middle East and North Africa. With assets of US$2,715bn at 31 December 2019, HSBC is one of the world's largest banking and financial services organisations.

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Consolidated Income Statement – GROUP 12 MONTHS ENDED 31 December 2019 and 2018

Figures in MXN millions

	Group	
	31 Dec 2019	**31 Dec 2018**
Interest income	67,841	59,305
Interest expense	(34,174)	(28,213)
Net interest income	33,667	31,092
Loan impairment charges	(9,149)	(8,884)
Risk-adjusted net interest income	24,518	22,209
Fees and commissions receivable	11,015	10,399
Fees payable	(3,277)	(2,761)
Trading income	4,706	3,123
Other operating income	2,250	1,469
Total operating income	39,212	34,438
Administrative and personnel expenses	(27,270)	(24,821)
Net operating income	11,942	9,617
Share of profits in equity interest	79	131
Profit/loss before tax	12,021	9,748
Income tax	(2,321)	(2,103)
Deferred income tax	(701)	(351)
Net income	8,999	7,294

Consolidated Income Statement – BANK 12 MONTHS ENDED 31 December 2019 and 2018

Figures in MXN millions

	Bank	
	31 Dec 2019	**31 Dec 2018**
Interest income	63,598	55,169
Interest expense	(32,217)	(25,783)
Net interest income	31,381	29,386
Loan impairment charges	(9,149)	(8,884)
Risk-adjusted net interest income	22,232	20,502
Fees and commissions receivable	10,473	9,819
Fees payable	(3,375)	(2,817)
Trading income	4,600	2,267
Other operating income	2,937	2,364
Total operating income	36,867	32,135
Administrative and personnel expenses	(27,062)	(24,664)
Net operating income	9,805	7,471
Share of profits in equity interest	76	179
Profit/loss before tax	9,881	7,650
Income tax	(1,826)	(1,512)
Deferred income tax	(681)	(302)
Net income	7,374	5,836

Consolidated Balance Sheet

	Group		Bank	
Figures in MXN millions	**31 Dec 2019**	**31 Dec 2018**	**31 Dec 2019**	**31 Dec 2018**
Assets				
Cash and deposits in banks	60,214	44,457	60,102	44,352
Margin accounts	680	525	680	525
Investment in securities	**183,549**	**220,167**	**168,072**	**203,367**
Trading securities	66,412	52,486	65,531	51,104
Available-for-sale securities	89,277	140,165	83,870	133,926
Held to maturity securities	27,860	27,516	18,671	18,337
Loan Securities	-	-		
Repurchase agreements	40,727	12,228	40,727	12,228
Derivative transactions	49,152	80,831	49,152	80,831
Performing loans				
Commercial loans	211,093	209,072	211,093	209,072
Loans to financial intermediaries	15,024	22,120	15,024	22,120
Loans to government entities	39,132	34,388	39,132	34,388
Consumer loans	64,362	58,606	64,362	58,606
Mortgage loans	63,070	47,553	63,070	47,552
Total performing loans	**392,681**	**371,739**	**392,681**	**371,738**
Impaired loans				
Commercial loans	4,067	4,580	4,067	4,580
Consumer loans	2,482	2,221	2,482	2,221
Mortgage loans	1,301	485	1,301	485
Total impaired loans	**7,850**	**7,286**	**7,850**	**7,286**
Gross loans and advances to customers	**400,531**	**379,025**	**400,531**	**379,024**
Allowance for loan losses	(13,182)	(12,903)	(13,182)	(12,903)
Net loans and advances to customers	**387,349**	**366,122**	**387,349**	**366,121**
Accounts receivables from Insurers and Bonding companies	61	61	-	
Premium receivables	1,779	1,582	-	-
Accounts receivables from reinsurers and rebonding companies	30	41	-	-
Benefits to be received from trading operations	-	94	-	94
Other accounts receivable	62,371	47,646	62,335	48,232
Foreclosed assets	379	396	379	396
Property, furniture and equipment, net	4,698	4,613	4,472	4,385
Long-term investments in equity securities	998	251	963	220
Long-term assets available for sale	249	27	240	27
Deferred taxes	10,974	13,219	10,832	13,045
Goodwill	1,048	1,048	-	-
Other assets, deferred charges and intangibles	4,722	4,240	4,569	4,033
Total assets	**808,980**	**797,548**	**789,872**	**777,856**

Consolidated Balance Sheet *(continued)*

	Group		Bank	
Liabilities	**31 Dec 2019**	**31 Dec 2018**	**31 Dec 2019**	**31 Dec 2018**
Deposits	**513,456**	**428,497**	**513,880**	**429,273**
Demand deposits	294,419	267,227	294,588	267,706
Time deposits	178,042	143,720	177,629	143,326
Bank bond outstanding	40,995	17,550	40,995	17,550
Global deposit account without movements		-	668	691
Bank deposits and other liabilities	**27,140**	**34,935**	**27,140**	**34,935**
On demand	91	2,000	91	2,000
Short-term	7,647	5,970	7,647	5,970
Long-term	19,402	26,965	19,402	26,965
Repurchase agreements	44,785	99,664	44,785	99,664
Stock Borrowing	-	-	-	-
Settlement accounts	-	-	-	-
Collateral sold	11,161	11,074	11,161	11,074
Derivative transactions	42,862	79,708	42,862	79,708
Technical reserves	12,684	12,543	-	-
Accounts payable from reinsures and rebounding companies	5	7	-	-
Other payable accounts	**69,642**	**52,458**	**69,267**	**51,902**
Income tax and employee profit sharing payable	1,163	716	1,149	519
Sundry creditors and other accounts Payable	68,479	51,742	68,118	51,383
Subordinated debentures outstanding	13,051	10,063	13,051	10,063
Deferred credits and receivable in advance	1,616	1,637	1,479	1,519
Total liabilities	**736,402**	**730,586**	**723,625**	**718,138**
Equity				
Paid in capital	**43,373**	**43,373**	**38,318**	**38,318**
Capital stock	6,218	6,218	6,132	6,132
Additional paid in capital	37,155	37,155	32,186	32,186
Other reserves	**29,198**	**23,582**	**27,925**	**21,396**
Capital reserves	1,244	1,244	12,474	11,891
Retained earnings	20,237	18,821	11,031	7,834
Result from the mark-to-market of available-for-sale securities	(1,105)	(3,403)	(1,148)	(3,232)
Result from cash flow hedging transactions	(177)	(374)	(177)	(374)
Adjustment in the employee pension			(1,629)	(559)
Net income	8,999	7,294	7,374	5,836
Minority interest in capital	7	7	4	4
Total equity	**72,578**	**66,962**	**66,247**	**59,718**
Total liabilities and equity	**808,980**	**797,548**	**789,872**	**777,856**

Consolidated Balance Sheet *(continued)*

	Group		Bank	
	31 Dec 2019	**31 Dec 2018**	**31 Dec 2019**	**31 Dec 2018**
Memorandum Accounts	**6,738,494**	**6,696,201**	**6,565,860**	**6,530,925**
Third party accounts	**27,541**	**27,033**	**26,041**	**25,303**
Clients current accounts	97	187	-	-
Custody operations	1,403	1,543	-	-
Third party investment banking operations, net	26,041	25,303	26,041	25,303
Proprietary position	**6,710,953**	**6,669,168**	**6,539,819**	**6,505,622**
Irrevocable lines of credit granted	341,647	311,120	341,647	311,120
Goods in trust or mandate	215,937	279,217	215,937	279,217
Goods in custody or under administration	1,251,071	1,085,412	1,244,853	1,079,194
Collateral received by the institution	64,637	48,862	64,637	48,862
Collateral received and sold or delivered as guarantee	25,190	34,215	25,190	34,215
Suspended interest on impaired loans	214	205	214	205
Other control accounts	4,812,257	4,910,137	4,647,341	4,752,809

Consolidated Statement of Changes in Shareholders' Equity

GROUP	Capital contributed	Capital reserves	Retained earnings	Result from valuation of available-for-sale securities	Result from cash flow hedging transactions	Net income	Minority interest	**Total equity**
Figures in MXN million								
Total Balances at 31 December 2018	**43,373**	**1,244**	**18,821**	**(3,403)**	**(374)**	**7,294**	**7**	**66,962**
Movements inherent to the shareholders' decision								
Transfer of result of prior years	-	-	7,294	-	-	(7,294)	-	**-**
Constitution of reserves	-	-		-	-	-	-	**-**
Cash dividends	-	-	(4,615)	-	-	-	-	**(4,615)**
Others		-	-	-	-	-	-	-
Total	**-**	**-**	**2,679**	**-**	**-**	**(7,294)**	**-**	**(4,615)**
Movements for the recognition of the comprehensive income								
Net income	-	-	-	-	-	8,999	-	**8,999**
Result from valuation of available-for-sale securities	-	-	-	2,298	-	-	-	**2,298**
Result from cash flow hedging transactions	-	-	-	-	197	-	-	**197**
Others *	-	-	(1,263)	-	-	-	-	**(1,263)**
Total	**-**	**-**	**(1,263)**	**2,298**	**197**	**8,999**	**-**	**10,231**
Total Balances at 31 December 2019	**43,373**	**1,244**	**20,237**	**(1,105)**	**(177)**	**8,999**	**7**	**72,578**

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

Consolidated Statement of Changes in Shareholders' Equity

BANK	Capital contributed	Capital reserves	Retained earnings	Result from valuation of available-for-sale securities	Result from cash flow hedging transactions	Adjustment in defined benefit pension plan	Net income	Minority interest	**Total equity**
Figures in MXN million									
Total Balances at 31 December 2018	**38,318**	**11,891**	**7,834**	**(3,232)**	**(374)**	**(559)**	**5,836**	**4**	**59,718**
Movements inherent to the shareholders' decision									
Transfer of result of prior years	-		5,836	-	-	-	(5,836)	-	**-**
Constitution of reserves	-	583	(583)	-	-	-	-	-	**-**
Cash dividends	-	-	(2,027)	-	-	-	-	-	**(2,027)**
Others	-	-	-	-	-	-	-	-	-
Total	**-**	**583**	**3,226**	**-**	**-**	-	**(5,836)**	**-**	**(2,027)**
Movements for the recognition of the comprehensive income									
Net income	-	-	-	-	-		7,374	-	**7,374**
Result from valuation of available-for-sale securities	-	-	-	2,084	-	-	-	-	**2,084**
Result from cash flow hedging transactions	-	-	-	-	197	-	-	-	**197**
Adjustment in defined benefit pension plan	-	-	(29)	-		(1,070)	-		**(1,099)**
Others	-	-	-	-	-	-	-	-	**-**
Total	**-**	**-**	**(29)**	**2,084**	**197**	**(1,070)**	**7,374**	**-**	**8,556**
Total Balances at 31 December 2019	**38,318**	**12,474**	**11,031**	**(1,148)**	**(177)**	**(1,629)**	**7,374**	**4**	**66,247**

Consolidated Statement of Cash Flows Group

Figures in MXN millions	**31 Dec 2019**
Net income	**8,999**
Adjustments for items not involving cash flow:	**18,470**
Allowances for loan losses	9,149
Depreciation and amortisation	1,618
Valuations	4,720
Technical reserves	(93)
Provisions	133
Income Tax and deferred taxes	3,022
Participation in the Results of Unconsolidated Subsidiaries	(79)
Changes in items related to operating activities:	
Margin accounts	(155)
Investment securities	39,895
Repurchase agreements	(28,499)
Derivative (assets)	27,191
Loan portfolio	(30,375)
Foreclosed assets	17
Benefits to be received from trading operations	94
Operating assets	(14,336)
Deposits	84,961
Bank deposits and other liabilities	(7,796)
Creditors repo transactions	(54,879)
Collateral sold or delivered as guarantee	87
Derivative (liabilities)	(36,846)
Subordinated debentures outstanding	2,988
Accounts receivables from reinsurers and coinsurers	9
Accounts receivables from premiums	(197)
Other operating liabilities	16,543
Income tax paid	(1,839)
Funds provided by operating activities	**24,332**
Investing activities:	
Proceeds on disposal of property, furniture and equipment	352
Acquisition of property, furniture and equipment	(1,835)
Intangible assets acquisitions & Prepaid expenses	(937)
Dividends	93
Proceeds on disposals of subsidiaries	712
Acquisition of subsidiaries	(1,425)
Other investment activities	(27)
Funds used in investing activities	**(3,067)**
Financing activities:	
Paid dividends	(4,615)
Other	(893)
Funds used in financing activities	**(5,508)**
Financing activities:	
Increase/decrease in cash and equivalents	15,757
Cash and equivalents at beginning of period	44,457
Cash and equivalents at end of period	**60,214**

Consolidated Statement of Cash Flows Bank

Figures in MXN millions	**31 Dec 2019**
Net income	**7,374**
Adjustments for items not involving cash flow:	**17,711**
Allowances for loan losses	9,149
Valuations	4,672
Depreciation	1,183
Amortisation	430
Provisions	(154)
Income Tax and deferred taxes	2,507
Share of profits in equity interest	(76)
Changes in items related to operating activities:	
Margin accounts	(155)
Investment securities	38,407
Repurchase agreements	(28,499)
Derivative (assets)	27,191
Loan portfolio	(30,375)
Benefits to be received from trading operations	94
Foreclosed assets	17
Operating assets	(15,494)
Deposits	84,607
Bank deposits and other liabilities	(7,796)
Creditors repo transactions	(54,879)
Collateral sold or delivered as guarantee	87
Derivative (liabilities)	(36,846)
Subordinated debentures outstanding	2,988
Other operating liabilities	16,942
Income tax paid	(1,286)
Funds provided by operating activities	**20,088**
Investing activities:	
Proceeds on disposal of property, furniture and equipment	352
Acquisition of property, furniture and equipment	(1,835)
Intangible assets acquisitions & Prepaid expenses	(1,012)
Proceeds on disposal of subsidiaries	531
Proceeds on disposal of permanent investments	712
Payments on disposal of permanent investments	(1,425)
Cash dividends	93
Other investment activities	273
Funds used in investing activities	**(2,311)**
Financing activities:	
Paid dividends	(2,027)
Funds used in financing activities	**(2,027)**
Financing activities:	
Increase/decrease in cash and equivalents	**15,750**
Cash and equivalents at beginning of period	44,352
Cash and equivalents at end of period	**60,102**

Changes in Mexican accounting standards

Introduction

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

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

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

i. Improvements of NIF 2019 issued by CINIF applicable to Financial Institutions.

CINIF issued a document called “Improvements of NIF 2019”, which mainly includes the following changes and improvements:

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

NIF B-9 “Interim Financial Reporting” – In order to converge with recent amendments to IAS 34 ‘Interim Financial Reporting’ originated by the implementation of IFRS 9 and IFRS 15, CINIF decided to amend NIF B-19 in same way including additional disclosures about fair value of financial instruments and revenue from contracts with customers. The accounting change has been in force since January 1st 2019, with a prospectively adoption.

Improvements which not originate accounting changes in Grupo Financiero HSBC.

NIF A-6 “Recognition and Measurement” – CINIF includes clarification about the meaning of ‘Net sale value’ indecating that it would be the cash flows obtain in the market by the sale or exchange of an asset less it is costs to sell.

NIF C-6 “Property, Plant and Equipment” – Changes to refer the determination of fair value of a fixed asset to the new NIF B-17 ‘Fair Value determination’ instead of NIF A-6 ‘Recognition and Measurement’ as it was set in older version.

NIF C-20 “Hold to Collect Financial Instruments” – Changes comprise clarifications in the accounting treatment of collaterals received by an entity, indecating that those shall not be recognised on balance sheet, unless they are cash or borrower is at default on his payment obligations.

NIF D-3 “Employee Benefits” – Several clarifications were included in wording of this standard to contribute in a better comprehension of the accounting implications when: i) there is a transfer of employees between entities under common control and ii) in case of changes in interest rate used (from governmental bonds rates to corporative bonds rates or vice versa) to determine the discount rate applicable to calculate ‘Defined Benefits Plans’ provisions.

NIF D-5 “Leases” – Clarifications about the determination of enforceable term of an agreement lease for lessee perspective and how a lessor should recognise payments from operating leases considering the pattern in which economic benefits from the asset would be obtained (accrual, straight line basis or other basis).

Regarding to the implementation of IFRS 9, IFRS 15 and IFRS 16 the expected date is January 1st, 2021 in accordance with last project sent by CNBV, for the rest of changes, the adoption date were January 1st 2019.

ii. New NIF B-11 'Disposal of non-current assets held for sale and discontinued operations'.

CINIF issued this new accounting standard with the purpose to separate the accounting treatment of 'Non-current Assets and Discontinued Operations' which mainly are focused on presentation and disclosure from 'Impairment of Assets' included in NIF C-15, in order to provided similarity with IFRS.

The following assets will be out of scope of NIF B-11, (only for measurement purposes, presentation and reclassification rules are applicable to all non-current assets):

- Biological assets (refers to NIF E-1 'Agriculture').
- Financial instruments (refers to NIF C-2 'Financial Instruments').
- Deferred taxes (refers to NIF D-4 'Income Taxes').
- Employee Benefit assets (refers to NIF D-3 'Employee Benefits').

In addition, NIF B-11 clarifies that assets in scope of this standard based on a liquidity presentation in balance sheet shall contemplate assets which recovery expectation is longer than 12 months.

This new standard will be in place since 2020 using a prospective approach in adoption, allowing an anticipated implementation. Given that Mexican Banking regulator has not issued an opinion about this new issuance and no financial impacts are expected, HSBC had no intention to anticipate its adoption.

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

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

In this context, in December 2017, the CNBV issued in the official gazette some specifications to be followed by Financial Institutions in the adoption of Mexican Accounting Standards "NIFs". It dectates that although those standards are in force since January 1st, 2018, Financial Institutions shall initially adopt them until January 1st 2019; nevertheless on November 15th 2018, CNBV issued a new adoption date until 2020. The latest change in adoption issued by CNBV, indecates that NIF would be adopted by Financial Institutions in 2021.

A summary of the content of those NIFs are described below:

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

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

NIF C-3 "Accounts receivable". It comprises the accounting rules of measurement, presentation and disclosures required for accounts receivables.

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

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

NIF C-16 "Impairment of financial instruments held to collect principal and interest". It comprises the measurement, accounting recognition, presentation and disclosures of the impairment of financial instruments hold to collect cash flows. It is important to highlight that the CNBV worked on special accounting standard which will cover the impairment for loans and advances that are held to collect cash flows, therefore this NIF would be partially adopted by Financial Institutions.

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

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

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

The NIF C-22 would be issued in 2020.

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

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

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

CNBV has sent to Banks different projects including proposal of changes in particular accounting standards applicable to Financial Institutions to match with the adoption of new NIF, nevertheless at the reporting date no final version has been issued on Official Gazette. Mainly changes are:

Loans and receivables:

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

According to last version of changes provided by CNBV, Financial Institutions would applied the use of effective interest rate until 2022, even if the rest of changes would be in force in 2021.

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

• New standard methodology to determine expected credit losses.

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

• Changes in regulatory reporting.

• A prospective adoption of these changes whose initial impacts should be recognised in 'Retained Earnings' category in share capital unless there is a different indecation.

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

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

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

Revocation of some particular accounting standards applicable to Financial Institutions:

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

B-2 Investment in financial instruments.
B-5 Derivatives and hedge accounting.
B-11 Collection rights.

C-1 Recognition and derecognition of financial assets.
C-3 Related parties.
C-4 Operating segment information.

When the new accounting standards are in place, Financial Institutions should replace the use of these particular accounting standards, adhering to new NIF.

Current expectation based on newest version is that these changes will be in force in 2021 (excepting by the use of effective interest rate method in measurement of loans which would be in force in 2022).

Currently, Grupo Financiero HSBC is evaluating the possible impacts originated by the adoption of these NIFs and changes in particular accounting standards applicable to Financial Institutions.

iv. Special accounting rules issued by National Banking Commission applicable to borrowers affected by natural disasters occurred during 2018.

On October 16th, 2018, the CNBV issued temporary special accounting rules (official response paper No. P-285/2018) “the programme” applicable to borrowers affected by natural disasters occurred from September to December 2018, as long as, their home address or the cash flows to pay the loan are located or originated in affected cities and states along Mexico that were declared by the Mexican Government as a disaster zone in the Official Gazette.

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

Basically, “the programme” brings an extension in loan term and skip payment of capital and interest accrued for a period no longer than three months (excepting by “microcreditos grupales” in which case the tenor would be extended for a longer period not exceeding 6 months). Each bank must decide if interests accrued during skip payment period are forgone or capitalised into the outstanding balance. The Bank has decided to apply a skip payment period forgoing the interest accrued. Under “the programme” loans modification would not be considered as restructured loan under CNBV accounting rules provisions.

Likewise, those loans modified would be considered as “performing loans” during skip payment period in order to determine their risk grade and loan impairment charges.

Based on the information aforementioned, at the end of reporting period, few customers have been adhered to the programme, therefore no relevant amount is shown, so far.

v. Special accounting rules issued by National Banking Commission applicable to borrowers affected by the new Federal Law of Wages applicable to Governmental Employees enacted on November 5th 2018.

On February 26th 2019, the CNBV issued temporary special accounting rules (official response paper No. P062/2019) “the benefit programme” applicable to borrowers affected by the enactment of the new Law which would produce a decrease in their wages or involuntary separation of their employment as long as this situation occurred between November 6th 2018 to September 30th 2019. The benefit programme would still be applicable when borrower acts as guarantor in loans.

These special accounting rules are applicable to consumer, and mortgages loans that were classified as “performing loans” at the date in which wages of borrowers decrease or their involuntary separation occurs as long as they adhered to the benefit programme no later than

February, 28th, 2020. In addition, the adherence to the benefit programme should be no later than 120 days after the event for loans originated from revolving credit facilities.

Basically, the benefit programme brings an extension in loan term and skip payment of capital and interest accrued for a period no longer than three months. Each bank must decide if interests accrued during skip payment period are forgone or capitalised into the outstanding balance. The Bank has decided to apply a skip payment period forgoing the interest accrued. Under "the benefit programme" loans modification would not be considered as restructured loan under CNBV accounting rules provisions.

At the end of reporting period, few customers have adhered to the benefit programme, therefore no relevant amount is shown, so far.

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

Grupo Financiero HSBC

HSBC Holdings plc, the ultimate parent of Grupo Financiero HSBC, reports its results under International Financial Reporting Standards (IFRS). Set out below is a reconciliation of the results of Grupo Financiero HSBC from Mexican GAAP to IFRS for the 12 months ended at 31 December of 2019 and an explanation of the key reconciling items.

	31 Dec 2019
Figures in MXN millions	
Grupo Financiero HSBC – Net Income Under Mexican GAAP	**8,999**
Differences arising from:	
Valuation of defined benefit pensions and post-retirement healthcare benefits, including post-employment benefits	48
Deferral of fees received and paid on the origination of loans and other effective interest rate adjustments	429
Loan impairment charges and other differences in presentation under IFRS	(61)
Recognition of the present value in-force of long-term insurance contracts	416
Other insurance adjustments[1]	(261)
Fair value adjustments on financial instruments	(125)
Deferred profit sharing	496
Other	(8)
Tax over adjustments	(216)
Net income under IFRS	**9,717**
Add back tax expense	3,513
Profit before tax under IFRS	**13,230**
Add back significant items	527
Adjusted net income before tax under IFRS	**13,757**
Significant items under IFRS:	
-Debit valuation adjustment on derivative contracts	152
-Restructuring cost	375
US dollar equivalent (millions):	
- Profit before tax under IFRS	**USD 702 Millions**
-Net income under IFRS	**USD 516 Millions**
Exchange rate used for conversion[2]	***18.8452***

[1] Includes technical reserves and effects from Solvency II

[2] Banxico rate at 31 December 2019

Summary of key differences between Grupo Financiero HSBC's results as reported under Mexican GAAP and IFRS

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

Mexican GAAP

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

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

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

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

IFRS

The main differences between Mex GAAP and IFRS comprise:

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

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

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

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

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

Mexican GAAP

The commissions charged to the borrower at loan inception are recorded into a deferred credit account (liability), which will be deferred against interest income in income statement on straight-line basis during contractual life of loan, excepting by those loans regarding to revolving credit facilities in which the deferral period is 12 months. In the case of commissions charged to borrowers for restructuring or renewals loans, they must be accumulated to the outstanding balance of commissions from original loan and deferring in interest income using the straight- line method during the new term of the loan.

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

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

IFRS

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

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

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

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

Loan impairment charges and other differences in presentation under IFRS

Mexican GAAP

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

Cash recoveries from written-off loans and the positive excess of loan impairment charges determined monthly were presented in Other Operating Income until December 2017. Since January 2018, Mexican Banking Regulator issued some changes in accounting standards that allow Banks to recognise either positive excess of loan impairment charges and/or cash recoveries from written-off loans as a credit adjustment in Loan Impairment Charges in the income statement.

IFRS

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

i. Credit-impaired (Stage 3)
ii. Purchased or originated credit-impaired (‘POCI’)
iii. Significant increase in credit risk (Stage 2)
iv. Stage 1 (the rest of the financial assets in scope not falling into any of the above categories).

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

Fair value adjustments on financial instruments

Mexican GAAP

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

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

IFRS

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

Deferred-profit sharing (PTU diferida)

Mexican GAAP

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

IFRS

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

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

Mexican GAAP

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

IFRS

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

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

Insurance liabilities and Insurance premiums recognised on an annualised basis

Mexican GAAP

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

Insurance premiums are recognised under annualisation criteria which is based in determine the total premium for the coverage period (1 year), consequently total premium is recognised since the moment where insurance contracts are written.

IFRS

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

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

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