HSBC Bank plc
Capital and Risk Management Pillar 3 Disclosures as at 31 December 2009

HSBC
The world's local bank

Contents

Tables

Capital and Risk Management Pillar 3 Disclosures as at 31 December 2009

Certain defined terms

This document comprises the Capital and Risk Management Pillar 3 Disclosures as at 31 December 2009 (‘Pillar 3 Disclosures 2009’) for HSBC Bank plc (‘the bank’) and its subsidiary undertakings (together ‘the group’). References to either ‘HSBC’ or ‘the Group’ within this document mean HSBC Holdings plc together with its subsidiaries.

Cautionary statement regarding forward-looking statements

These *Pillar 3 Disclosures 2009* contain certain forward-looking statements with respect to the financial condition, results of operations and business of the group. Statements that are not historical facts, including statements about the group’s beliefs and expectations, are forward-looking statements. Words such as ‘expects’, ‘anticipates’, ‘intends’, ‘plans’, ‘believes’, ‘seeks’, ‘estimates’, ‘potential’ and ‘reasonably possible’, variations of these words and similar expressions are intended to identify forward-looking statements. These statements are based on current plans, estimates and projections, and therefore undue reliance should not be placed on them. Forward-looking statements speak only as of the date they are made, and it should not be assumed that they have been revised or updated in the light of new information or future events.

Introduction

The bank is a subsidiary of HSBC Holdings plc. HSBC is one of the largest banking and financial services organisations in the world, with a market capitalisation of US$199 billion at 31 December 2009.

Through its subsidiaries and associates, HSBC provides a comprehensive range of banking and related financial services. Headquartered in London, HSBC operates through long-established businesses and has an international network of some 8,000 properties in 88 countries and territories in six geographical regions: Europe; Hong Kong; Rest of Asia-Pacific; the Middle East; North America and Latin America. Within these regions, a comprehensive range of financial services is offered to personal, commercial, corporate, institutional, investment and private banking clients. Services are delivered primarily by domestic banks, typically with large retail deposit bases, and by consumer finance operations.

Details of HSBC’s principal activities and its strategic direction can be found on page 12 of the HSBC Holdings plc *Annual Report and Accounts* 2009.

The group provides a comprehensive range of banking and related financial services. The group divides its activities into business segments: UK Retail Banking; Continental Europe Retail Banking; Global Banking and Markets; and Private Banking.

The group has an extensive branch network, predominantly across Europe. As at 31 December 2009, the bank had 1,369 branches in the United Kingdom, and 14 branches in the Isle of Man and the Channel Islands.

Details of the group’s principal activities can be found on page 3 of the HSBC Bank plc *Annual Report and Accounts 2009.*

Basel II

The Financial Services Authority of the United Kingdom (‘FSA’) supervises the group on a consolidated basis and certain individual businesses separately, e.g. the bank. It receives information on the capital adequacy of, and sets capital requirements for, these individual businesses and the group as a whole. Individual banking subsidiaries are directly regulated by their local banking supervisors, who set and monitor their capital adequacy requirements.

Basel II is structured around three ‘pillars’: minimum capital requirements, supervisory review and market discipline. The Capital Requirements Directive (‘CRD’) implemented Basel II in the European Union (‘EU’) and the FSA then gave effect to the CRD by including the requirements of the CRD in its own rulebooks – particularly its main prudential sourcebooks for the banking industry, GENPRU & BIPRU.

Pillar 3 disclosures 2009

Pillar 3 complements the minimum capital requirements and the supervisory review process. Its aim is to encourage market discipline by developing a set of disclosure requirements which allow market participants to assess certain specified information on: the scope of application of Basel II, capital, particular risk exposures and risk assessment processes, and hence the capital adequacy of the institution. Disclosures consist of both quantitative and qualitative information and are provided at the consolidated level.

Banks are required to disclose all their material risks as part of the pillar 3 framework. All material and non-proprietary information required by pillar 3 is included in the HSBC Holdings plc *Pillar 3 Disclosures 2009*. HSBC Bank plc, as a significant subsidiary of HSBC Holdings plc, is required to publish certain limited pillar 3 disclosures separately.

The FSA permits certain pillar 3 requirements to be satisfied by inclusion within a firm's financial statements. Where this is the case, this document provides page references to the relevant sections in the HSBC Bank plc *Annual Report and Accounts 2009* and HSBC Holdings plc *Annual report and Accounts 2009.*

Future Developments

The regulation and supervision of financial institutions is currently undergoing a period of significant change in response to the global financial crisis. An overview of the risks associated with regulatory reform is presented on page 16 of the HSBC Holdings plc *Annual report and Accounts 2009*.

Increased capital requirements and pillar 3 disclosures for market risk and securitisations have already been announced by the Basel Committee and are due for implementation in the EU in 2011. The Basel Committee issued further proposals in a Consultative Document 'Strengthening the resilience of the banking sector' on 17 December 2009. The Committee's proposals are part of global initiatives to strengthen the financial regulatory system, and have been endorsed by the Financial Stability Board and the G20 leaders. A comprehensive impact assessment will be carried out on the proposals in the first half of 2010, with the aim of developing a fully calibrated set of standards by the end of 2010. The proposals will be phased in as financial conditions improve and economic recovery is assured, with the aim of implementation by the end of 2012. Within this context, the Basel Committee will also consider appropriate transition and grandfathering arrangements. The consultation period for these proposals closes on 16 April 2010.

Frequency

In accordance with FSA requirements, the bank intends to publish its pillar 3 disclosures annually.

Media and location

The HSBC Holdings plc *Pillar 3 Disclosures 2009* and other information on the Group are available on HSBC's investor relations website: www.hsbc.com/investor-relations.

Comparison with the HSBC Bank plc *Annual Report and Accounts 2009*

The *Pillar 3 Disclosures 2009* have been prepared in accordance with regulatory capital adequacy concepts and rules, rather than in accordance with International Financial Reporting Standards ('IFRSs'). Therefore, some information in the *Pillar 3 Disclosures 2009* is not directly comparable with the financial information in the HSBC Bank plc *Annual Report and Accounts 2009*. This is most pronounced for the credit risk disclosures, where credit exposure is defined as the maximum loss the Group has estimated under specified Basel II parameters. This differs from similar information in the HSBC Bank plc *Annual Report and Accounts 2009*, which is mainly reported as at the balance sheet date and, therefore, does not reflect the likelihood of future drawings of committed credit lines.

Verification

The *Pillar 3 Disclosures 2009* have been verified internally but have not been audited by the group's external auditor.

Consolidation basis

The basis of consolidation for financial accounting purposes is described on page 41 of the HSBC Bank plc *Annual Report and Accounts 2009.* This differs from that used for regulatory purposes. Investments in banking associates, which are equity accounted in the financial accounting consolidation, are proportionally consolidated for regulatory purposes. Subsidiaries and associates engaged in insurance and non-financial activities are excluded from the regulatory consolidation and are deducted from regulatory capital. The regulatory consolidation does not include Special Purpose Entities ('SPEs') where significant risk has been transferred to third parties. Exposures to these SPEs are either risk-weighted as securitisation positions or deducted from capital for regulatory purposes.

Scope of Basel II permissions

Credit risk

Basel II provides three approaches of increasing sophistication to the calculation of minimum credit risk capital requirements. The most basic, the standardised approach, requires banks to use external credit ratings to determine the risk weightings applied to rated counterparties, to classify counterparties into broad categories and to apply standardised risk weightings. The next level, the internal ratings-based ('IRB') foundation approach, allows banks to calculate their credit risk capital requirements on the basis of their internal assessment of the probability that a counterparty will default ('PD'), but uses supervisory formulae to estimate exposure at default ('EAD') and loss given default ('LGD'). Finally, the IRB advanced approach allows banks to use their own internal assessment in both determining PD and quantifying EAD and LGD.

The capital resources requirement, which is intended to cover unexpected losses, is derived from a formula specified in the regulatory rules, which incorporates these factors and other variables such as maturity and correlation. Expected losses under the IRB approaches are calculated by multiplying PD by EAD and LGD. Expected losses are deducted from capital to the extent that they exceed accounting impairment allowances on the IRB portfolios.

For credit risk, with the FSA's approval, the group has adopted the IRB advanced approach for the majority of its business, with the remainder on either IRB foundation or standardised approaches. A rollout plan is in place to extend coverage of the advanced approach over the next few years for both local and consolidated group reporting, leaving a small residue of exposures on the standardised approach. In December 2009, corporate portfolios in France completed the transition from foundation to advanced IRB approach.

Counterparty credit risk

Counterparty credit risk in both the trading and non-trading books is the risk that the counterparty to a transaction may default before completing the satisfactory settlement of the transaction.

Three methods for determining exposure values are defined by Basel II: standardised, mark-to-market and internal model method. These exposure values are used to determine capital requirements under one of the credit risk approaches; standardised, IRB foundation and IRB advanced.

The group uses the mark-to-market and internal model methods for counterparty credit risk. Its longer-term aim is to migrate more positions from the mark-to-market to the internal model method.

Market risk

Market risk is the risk that movements in market risk factors, including foreign exchange rates, commodity prices, interest rates, credit spreads and equity prices will reduce the group's income or the value of its portfolios. Market risk is measured, with FSA permission, using Value at Risk ('VAR') models or the standard market risk PRR (Position Risk Requirement) rules prescribed by the FSA.

The group uses both approaches for market risk. Its longer-term aim is to migrate more positions from standard market risk PRR rules to VAR.

Operational risk

Basel II includes capital requirements for operational risk, again utilising three levels of sophistication. The capital required under the basic indicator approach is a simple percentage of gross revenues, whereas under the standardised approach it is one of three different percentages of gross revenues allocated to each of eight defined business lines. Both these approaches use an average of the last three financial years' revenues. Finally, the advanced measurement approach uses a bank's own statistical analysis and modelling of operational risk data to determine capital requirements.

The group has adopted the standardised approach in determining its operational risk capital requirements.

Capital

Table 1: Capital structure at 31 December 2009

	At 31 December 2009	At 31 December 2008
Composition of regulatory capital	**£m**	£m restated [1]
Shareholders' equity [2]	**32,248**	28,985
Shareholders' equity per balance sheet	**27,787**	19,923
Preference shares & related premium [3]	**(431)**	(431)
Other equity instruments [3]	**(1,750)**	(1,750)
Deconsolidation of special purpose entities [4]	**6,642**	11,243
Minority Interests	**641**	738
Regulatory adjustments to the accounting basis …	**(562)**	(2,144)
Unrealised (gains)/losses on available-for-sale debt securities [5]	**(109)**	825
Own credit spread	**(168)**	(365)
Defined benefit pension fund adjustment [6]	**695**	(469)
Cash flow hedging reserve	**(350)**	(327)
Reserves arising from revaluation of property & unrealised gains on available-for-sale equities	**(480)**	(341)
Other regulatory adjustments	**(150)**	(1,467)
Deductions	**(11,518)**	(12,011)
Goodwill capitalised & intangible assets	**(10,560)**	(11,239)
50% of securitisation positions	**(514)**	(318)
50% of excess expected losses over impairment allowances	**(616)**	(640)
50% of tax credit adjustment for excess expected losses	**172**	186
Core tier 1 capital	**20,809**	15,568
Other tier 1 capital before deductions	**2,241**	2,220
Preference shares & related premium [3]	**431**	431
Innovative tier 1 securities [3]	**1,810**	1,789
Deductions	**(343)**	(265)
Unconsolidated investments [7]	**(515)**	(451)
50% of tax credit adjustment for excess expected losses	**172**	186
Tier 1 capital	**22,707**	17,523
Total qualifying tier 2 capital before deductions	**11,272**	11,442
Reserves arising from unrealised gains on revaluation of property & available-for-sale equities	**480**	342
Collective impairment allowances [8]	**368**	-
Perpetual subordinated debt [3]	**3,320**	3,451
Term subordinated debt [3]	**7,104**	7,649
Total deductions other than from tier 1 capital	**(2,139)**	(1,867)
Unconsolidated investments [7]	**(1,004)**	(899)
50% of securitisation positions	**(514)**	(318)
50% of excess expected losses over impairment allowances	**(616)**	(640)
Other deductions	**(5)**	(10)
Total regulatory capital	**31,840**	27,098
Composition of regulatory capital - supplementary analysis	**£m**	£m
Tier 1 capital		
Total tier 1 capital excluding innovative tier 1 securities	**20,897**	15,734
Tier 1 Capital	**22,707**	17,523
Less innovative tier 1 securities [3]	**(1,810)**	(1,789)
Tier 2 capital		
Total tier 2 capital before deductions plus innovative tier 1 securities	**13,082**	13,231
Total qualifying tier 2 capital before deductions	**11,272**	11,442
Innovative tier 1 securities [3]	**1,810**	1,789
Total deductions other than from tier 1 capital	**(2,139)**	(1,867)
Total regulatory capital	**31,840**	27,098

Capital and Risk Management Pillar 3 Disclosures as at 31 December 2009

Table 1: Capital structure at 31 December 2009 (continued)

	At 31 December 2009		At 31 December 2008	
Capital requirements	**RWA £m**	**Capital required £m**	RWA £m	Capital required £m
Credit risk and counterparty risk	**167,259**	**13,381**	211,206	16,897
Market risk	**12,655**	**1,012**	25,311	2,025
Operational risk	**23,367**	**1,869**	21,366	1,709
Total capital requirements	**203,281**	**16,262**	257,883	20,631
Capital ratios		**%**		%
Core tier 1 capital		**10.2**		6.0
Tier 1 capital		**11.2**		6.8
Total capital		**15.7**		10.5

Notes

1 *In May 2009 the FSA confirmed changes to the definition of core tier 1 capital for disclosure purposes. HSBC Bank's core tier 1 capital for December 2008 has been restated accordingly for comparison.*
2 *Includes externally verified profits for the year to 31 December 2009.*
3 *Details of the terms and conditions of subordinated liabilities and other equity instruments can be found on page 116 and pages 130-131 of the HSBC Bank plc Annual Report and Accounts 2009.*
4 *Mainly comprises unrealised losses on available-for-sale debt securities owned by deconsolidated special purpose entities.*
5 *Under FSA rules unrealised gains/losses on available-for-sale debt securities must be excluded from capital resources.*
6 *FSA rules permit banks to replace a liability in a defined benefit pension scheme by the additional funding that will be paid into the scheme over a 5 year period.*
7 *Mainly comprise investment in insurance entities.*
8 *Under Basel II rules collective impairment allowances on loan portfolios under the standardised approach may be included in tier 2 capital.*

Internal assessment of capital adequacy

The group assesses the adequacy of its capital by considering the resources necessary to cover unexpected losses arising from discretionary risks, being those which it accepts (such as credit risk and market risk), or non-discretionary risks, being those which arise by virtue of its operations (such as operational risk and business risk). The Group Capital Management Principles and related policies define the Internal Capital Adequacy Assessment Process ('ICAAP') by which senior management and the Board of Directors of HSBC Bank plc ('the Board') examine the risk profile from both regulatory and economic capital viewpoints and ensure that the group's level of capital:

- remains sufficient to support the group's risk profile and outstanding commitments;
- exceeds the group's formal minimum regulatory capital requirements by an agreed margin;
- is capable of withstanding a severe economic downturn stress scenario; and
- remains consistent with the group's strategic and operational goals, and shareholder and rating agency expectations.

The regulatory and economic capital assessments rely upon the use of models that are integrated into the group's management of risk.

Economic capital is the internally calculated capital requirement which the group deems necessary to support the risks to which it is exposed. It is set at a confidence level consistent with a target credit rating of AA. Regulatory capital is the capital which the group is required to hold by the rules established by the FSA for the consolidated group and by local regulators for individual group companies.

The economic capital assessment is the more risk-sensitive measure as it covers a wider range of risks and takes account of the substantial diversification of risk accruing from the group's operations. The group's economic capital models, based on those developed by the Group, are calibrated to quantify the level of capital that is sufficient to absorb potential losses over a one-year time horizon to a 99.95 per cent level of confidence for its banking activities and to a 99.5 per cent level of confidence for its insurance activities and pension risks. The group's approach to capital management is aligned to its corporate structure, business model and strategic direction.

The group's discipline around capital allocation is maintained within established processes and benchmarks, in particular the approved annual group capital plan.

Regulatory and economic capital are the metrics by which risk is measured and linked to capital within the group's risk appetite framework. The framework, which expresses the types and quantum of risks to which the group wishes to be exposed, is approved and monitored by the Board and senior management.

The group identifies and manages risk through a defined risk management framework and continuous monitoring of the risk environment. It assesses and manages certain of these risks via the capital planning process. Risks assessed via capital and those that are not are compared below.

Risks assessed via capital

Credit (including counterparty credit), market and operational risk

The group assesses economic capital requirements for these risk types utilising the embedded operational infrastructure used for the calculation of minimum capital requirements, together with an additional suite of models that take into account, in particular:

- the increased level of confidence required to meet the group's strategic goals (99.95 per cent); and
- internal assessments of diversification of risks within the group's portfolios and, similarly, any concentrations of risk that arise.

The group's economic capital assessment operates alongside the group's regulatory capital reporting process and consistently demonstrates a substantially lower overall capital requirement for credit risk than the regulatory equivalent, evidencing the benefits of European diversification. However, the group maintains a prudent stance on capital coverage, ensuring that any model risk is mitigated. Economic capital requirements are used to monitor the group's risks against its risk appetite.

Interest rate risk in the banking book

Interest rate risk in the banking book ('IRRBB') is defined as the exposure of the non-trading products of the group to interest rates. Non-trading portfolios include positions that arise from the interest rate management of the group's retail and commercial banking assets and liabilities, and financial investments designated as available-for-sale or held-to-maturity. IRRBB arises principally from mismatches between the future yields on assets and their funding costs, as a result of interest rate changes. Analysis of this risk is complicated by having to make assumptions on embedded optionality in certain products, e.g. the incidence of mortgage prepayments, and by the inclusion of behavioural assumptions regarding the economic duration of liabilities which are contractually repayable on demand, e.g. current accounts. IRRBB economic capital is defined as the amount of capital necessary to cover an unexpected loss in value of the group's non-trading products over one year to a 99.95 per cent level of confidence.

Insurance risk

The group operates a bancassurance model which provides insurance products for customers with whom the group has a banking relationship. Many of these insurance products are manufactured by group subsidiaries but, where the group considers it operationally more effective, third parties are engaged to manufacture and provide insurance products which the group sells through its banking network. The group works with a limited number of market-leading partners to provide these products. When manufacturing products, the group underwrites the insurance risk and retains the risks and rewards associated with writing insurance contracts.

Significant progress has been made towards finalising a risk-based capital methodology for the group's insurance businesses. Pending implementation across the group, a Net Asset Value capital deduction methodology is being employed for economic capital assessment purposes.

Pension risk

The group operates a number of pension plans. Some of these are defined benefit plans, of which the largest is the HSBC Bank (UK) Pension Scheme. The benefits payable under the defined benefit plans are typically a function of salary and length of service. In order to fund these benefits, sponsoring group companies (and in some instances, employees) make regular contributions in accordance with advice from actuaries and in consultation with the scheme's trustees (where relevant). The defined benefit plans invest these contributions in a range of investments designed to meet their long-term liabilities.

Capital and Risk Management Pillar 3 Disclosures as at 31 December 2009

Pension risk arises from the potential for a deficit in a defined benefit plan to arise from a number of factors, which could include:

- investments delivering a return below that required to provide the projected plan benefits. This could arise, for example, when there is a fall in the market value of equities, or when increases in long-term interest rates cause a fall in the value of fixed income securities held;
- the prevailing economic environment leading to corporate failures, thus triggering write-downs in asset values (both equity and debt);
- a change in either interest rates or inflation which causes an increase in the value of the scheme liabilities; and
- scheme members living longer than expected (known as longevity risk).

Pension risk is assessed by way of an economic capital model that takes into account potential variations in these factors, using a VAR model.

Residual risk

Residual risk is primarily the risk that mitigation techniques prove less effective than expected. This category also includes risks that arise from specific reputational or business events that give rise to exposures not deemed to be included in the major risk categories. The group conducts economic capital assessments of such risks on a regular, forward-looking basis to ensure that their impact is adequately covered by its capital base.

Risks not explicitly assessed via capital

Liquidity risk

Liquidity and funding risk management is described in detail on pages 148-151 of the HSBC Bank plc *Annual Report and Accounts 2009.*

The group uses cash-flow stress testing as part of its control processes to assess liquidity risk. The group does not manage liquidity through the explicit allocation of capital as, in common with standard industry practice, this is not considered to be an appropriate or adequate mechanism for managing these risks. However, the group recognises that a strong capital base can help to mitigate liquidity risk both by providing a capital buffer to allow an entity to raise funds and deploy them in liquid positions and by serving to reduce the credit risk taken by providers of funds to the group.

Structural foreign exchange risk

Structural foreign exchange risks arise from the group's net investments in subsidiaries, branches and associates, the functional currencies of which are other than sterling. Unrealised gains or losses due to revaluation of structural foreign exchange exposures are reflected in reserves, whereas other unrealised gains or losses arising from revaluation of foreign exchange positions are reflected in the income statement.

The group's structural foreign exchange exposures are managed with the primary objective of ensuring, where practical, that the group's consolidated capital ratios and the capital ratios of the individual banking subsidiaries are largely protected from the effect of changes in exchange rates. This is usually achieved by ensuring that, for each subsidiary bank, the ratio of structural exposures in a given currency to risk-weighted assets ('RWA') denominated in that currency is broadly equal to the capital ratio of the subsidiary in question. The group does not assign economic capital to any residual structural foreign exchange exposures, since they are managed within appropriate economic capital buffers.

Details of the group's management of structural foreign exchange risk can be found on page 156 of the HSBC Bank plc *Annual Report and Accounts 2009.*

Reputational risk

Details of the group's management of reputational risk can be found on page 23 of the HSBC Bank plc *Annual Report and Accounts 2009.*

As a banking group, the group's reputation depends upon the way in which it conducts its business, but it can also be affected by the way in which clients to whom it provides financial services conduct themselves. A Group Reputational Risk Committee was established in 2008, at which Group functions with responsibility for activities that attract reputational risk are represented.

Sustainability risk

Sustainability (environmental and social) risks arise from the provision of financial services to companies or projects which run counter to the needs of sustainable development. The group follows HSBC's framework for the management of sustainability risk, a description of which can be found on page 264 of the HSBC Holdings plc *Annual Report and Accounts 2009.*

Business risk

The FSA specifies that banks, as part of their internal assessment of capital adequacy process, should review their exposure to business risk.

Business risk is the potential negative impact on profits and capital as a result of the group not meeting its strategic objectives, as set out in the rolling operating plan, owing to unforeseen changes in the business and regulatory environment, exposure to economic cycles and technological changes. The group does not explicitly set aside capital against business risk as a distinct category as it believes that this risk is effectively covered by the capital set aside for other major risks such as credit risk, market risk and operational risk.

Scenario analysis and stress testing

Scenario analysis and stress testing are important mechanisms in understanding the sensitivities of the group's business and capital plans to the adverse effects of a range of plausible events of varying severity, some of which are extreme. As well as considering the potential financial impact upon plans, a key output of this tool is the consideration and establishment of management action plans for mitigating such events should they, or similar events, arise.

Regulatory capital supply is regularly assessed against demand under a range of stress scenarios, including projected global and local economic downturns. Qualitative and quantitative techniques are used to estimate the potential impact on the group's capital position under such scenarios. The group also participates, where appropriate, in standard scenario analyses requested by regulatory bodies.

In addition to macro-economic analysis, event-driven scenarios, including operational, market and credit events, are regularly formulated and analysed in detail, ensuring that management has considered their potential impact, and what actions would be necessary, should a range of risks materialise.

In particular, this framework has aided management in mitigating some of the effects of the global financial crisis. While the prediction of future events cannot cover all eventualities, nor precisely identify future events, a number of the scenarios analysed in the past provided additional management insight into the actions necessary to mitigate the risks when similar events occurred.

As part of the group's risk appetite process, business and capital plans are supported by forecasts of the risk parameters that drive the group's capital requirements. The group carries out macro-economic stress tests which consider sensitivities of these drivers under a variety of potential economic forecasts in order to examine the possible capital positions that could arise. In any material economic downturn, proactive and structured intervention by management is both inevitable and necessary. Therefore, the group incorporates the effect of such management actions in determining whether or not it is likely to be able to withstand such an event.

Credit risk and market risk

The following page sets out credit and market risk-weighted assets and regulatory capital requirements as at 31 December 2009.

Capital and Risk Management Pillar 3 Disclosures as at 31 December 2009

Table 2: Credit risk – summary

	At 31 December 2009		At 31 December 2008	
Total credit risk capital requirements	**Capital required £m**	**RWA £m**	Capital required £m	RWA £m
Credit risk	**11,918**	**148,969**	14,399	179,980
Counterparty credit risk	**1,463**	**18,290**	2,498	31,226
Total	**13,381**	**167,259**	16,897	211,206
Credit risk analysis by exposure class				
Exposures under the IRB advanced approach	**7,470**	**93,373**	7,848	98,093
Retail:				
– secured on real estate property	**601**	**7,509**	588	7,353
– qualifying revolving retail	**622**	**7,779**	475	5,939
– small and medium-sized enterprises	**310**	**3,883**	366	4,574
– other retail	**588**	**7,346**	779	9,729
Total retail	**2,121**	**26,517**	2,208	27,595
Central governments and central banks	**122**	**1,527**	107	1,335
Institutions	**579**	**7,231**	949	11,868
Corporates	**3,976**	**49,697**	3,872	48,394
Securitisation positions [1]	**672**	**8,401**	712	8,901
Exposures under the foundation IRB approach	**214**	**2,668**	1,812	22,652
Corporates	**214**	**2,668**	1,812	22,652
Exposures under the Standardised approach	**4,234**	**52,928**	4,739	59,235
Institutions	**577**	**7,211**	499	6,241
Corporates	**2,035**	**25,444**	2,455	30,677
Retail	**313**	**3,907**	427	5,342
Secured on real estate property	**322**	**4,027**	309	3,865
Past due items	**62**	**774**	20	248
Regulatory high-risk categories	**-**	**-**	19	241
Collective investment undertakings	**11**	**143**	-	-
Other items than equity [2]	**539**	**6,737**	649	8,106
Equity – Institutions	**11**	**138**	12	150
Equity - Other	**364**	**4,547**	349	4,365
Total	**11,918**	**148,969**	14,399	179,980

Table 3: Market risk capital requirements

	At 31 December 2009		At 31 December 2008	
Market Risk	**Capital required £m**	**RWA £m**	Capital required £m	RWA £m
Interest rate position risk requirement [3]	**146**	**1,823**	338	4,225
Equity position risk requirement [3]	**7**	**89**	15	188
Commodity position risk requirement [3]	**5**	**57**	7	91
Foreign exchange position risk requirement [3]	**4**	**56**	14	178
VAR requirement	**850**	**10,630**	1,651	20,629
Total market risk capital requirement	**1,012**	**12,655**	2,025	25,311

Notes

1 *Excludes securitisation positions deducted from capital (which would otherwise be risk-weighted at 1,250 per cent). Securitisation positions deducted from capital are shown in Table 1.*

2 *Includes immaterial exposures to central governments & central banks, regional governments & local authorities, and administrative bodies & non-commercial undertakings, in addition to items such as tangible fixed assets, prepayments and deferred taxation.*

3 *Calculated using FSA standard market risk PRR rules.*

Glossary

Terms	Definition
Available-for-sale financial assets	Those non-derivative financial assets that are designated as available for sale or are not classified as a) loans and receivables b) held-to-maturity investments or c) financial assets at fair value through profit or loss.
Basel II	The capital adequacy framework issued by the Basel Committee on Banking Supervision in June 2006 in the form of the 'International Convergence of Capital Measurement and Capital Standards'.
BIPRU	The FSA's rules, as set out in Prudential Sourcebook for Banks, Building Societies and Investment Firms.
Core tier 1 capital	The highest quality form of regulatory capital. It comprises total shareholders' equity and related minority interests, less goodwill and intangible assets, and certain other regulatory adjustments.
Derivatives	A derivative is a financial instrument whose value is based on the performance of one or more underlying assets, for example bonds or currencies.
ECAI	External Credit Assessment Institution, such as Moody's Investors Service, Standard & Poor's Ratings Group or Fitch Group.
Economic capital	The internally calculated capital requirement which is deemed necessary by the group to support the risks to which it is exposed at a confidence level consistent with a target credit rating of AA.
Expected loss ('EL') (regulatory)	A regulatory measure of the amount expected to be lost on an exposure using a 12 month time horizon and downturn loss estimates. EL is calculated by multiplying the Probability of Default (a percentage) by the Exposure at Default (an amount) and Loss Given Default (a percentage).
Exposure	A claim, contingent claim or position which carries a risk of financial loss.
Exposure at default ('EAD') and Exposure value	The amount expected to be outstanding after any credit risk mitigation, if and when a counterparty defaults. EAD reflects drawn balances as well as allowance for undrawn amounts of commitments and contingent exposures, and is usually measured over a 12 month horizon.
Fair value	Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.
FSA	The Financial Services Authority of the United Kingdom.
GENPRU	The FSA's rules, as set out in the General Prudential Sourcebook.
Held-to-maturity	An accounting classification for investments acquired with the intention of being held until they mature.
Institutions	Under the Standardised approach, Institutions are classified as credit institutions or investment firms. Under the IRB approach, Institutions also include regional governments and local authorities, public sector entities and multilateral development banks.
Insurance risk	A risk, other than financial risk, transferred from the holder of a contract to the insurance provider. The principal insurance risk is that, over time, the combined cost of claims, administration and acquisition of the contract may exceed the aggregate amount of premiums received and investment income.
Internal Capital Adequacy Assessment Process ('ICAAP')	The group's own assessment of the levels of capital that it needs to hold through an examination of its risk profile from regulatory and economic capital viewpoints.

Glossary

Terms	Definition
Internal ratings-based approach ('IRB')	A method of calculating credit risk capital requirements using internal, rather than supervisory, estimates of risk parameters.
IRB advanced approach	The IRB advanced approach is a method of calculating credit risk capital requirements using internal PD, LGD and EAD models.
IRB foundation approach	The IRB foundation approach is a method of calculating credit risk capital requirements using internal PD models but supervisory estimates of LGD and conversion factors for the calculation of EAD.
Loss given default ('LGD')	The estimated ratio (percentage) of the economic loss on an exposure to the amount outstanding at default (EAD) upon default of a counterparty.
Probability of default ('PD')	The probability that an obligor will default within a one-year time horizon.
Qualifying revolving retail exposures	Retail IRB exposures not exceeding €100k that are revolving, unsecured, and (to the extent they are not drawn) immediately and unconditionally cancellable, such as credit cards.
Regulatory capital	The capital which the bank holds, determined in accordance with rules established by the FSA for the consolidated group and by local regulators for individual group companies.
Retail IRB	Retail exposures that are treated under the IRB approach.
Risk appetite	An assessment of the types and quantum of risks to which HSBC wishes to be exposed.
Risk-weighted assets ('RWA')	Calculated by assigning a degree of risk expressed as a percentage (risk weight) to an exposure in accordance with the applicable Standardised or IRB approach rules.
Securitisation	A transaction or scheme whereby the credit risk associated with an exposure, or pool of exposures, is tranched and where payments to investors in the transaction or scheme are dependent upon the performance of the exposure or pool of exposures. A traditional securitisation involves the transfer of the exposures being securitised to an SPE which issues securities. In a synthetic securitisation, the tranching is achieved by the use of credit derivatives and the exposures are not removed from the balance sheet of the originator.
Special Purpose Entity ('SPE')	A corporation, trust or other non-bank entity, established for a narrowly defined purpose, including for carrying on securitisation activities. The structure of the entity and activities are intended to isolate the obligations of the SPE from those of the originator and the holders of the beneficial interests in the securitisation.
Standardised approach	In relation to credit risk, a method for calculating credit risk capital requirements using ECAI ratings and supervisory risk weights. In relation to operational risk, a method of calculating the operational capital requirement by the application of a supervisory defined percentage charge to the gross income of eight specified business lines.
Standard market risk PRR rules	The FSA's rules regarding the calculation of market risk capital requirements for trading book exposures which are not subject to VAR model permissions. The rules divide risks into a number of standard types, within which risk is measured by the application of defined percentage charges to both net & gross exposures.

Glossary

Terms	Definition
Tier 1 capital	A component of regulatory capital, comprising core tier 1 capital and other tier 1 capital. Other Tier 1 capital includes qualifying hybrid capital instruments such as non-cumulative perpetual preference shares and innovative Tier 1 securities.
Tier 2 capital	A component of regulatory capital comprising qualifying subordinated loan capital, related minority interests, allowable collective impairment allowances and unrealised gains arising on the fair valuation of equity instruments held as available-for-sale. Tier 2 capital also includes reserves arising from gains on the revaluation of properties.
Value at risk (‘VAR’)	A technique that measures the loss that could occur on risk positions as a result of adverse movements in market risk factors (e.g. rates, prices, volatilities) over a specified time horizon and to a given level of confidence.

The world's local bank

HSBC Bank plc
8 Canada Square
London E14 5HQ
United Kingdom
Telephone: 44 020 7991 8888
Facsimile: 44 020 7992 4880