

HSBC HOLDINGS PLC  
Form 6-K  
August 03, 2007

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**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

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**FORM 6-K**

**REPORT OF FOREIGN PRIVATE ISSUER PURSUANT TO RULE 13a-16 OR 15d-16 OF  
THE SECURITIES EXCHANGE ACT OF 1934**

For the month of August, 2007

**HSBC Holdings plc**

42nd Floor, 8 Canada Square,  
London E14 5HQ,  
England

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Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F.

Form 20-F

Form 40-F

Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to Rule 12g3-2(b) under the Securities Exchange Act of 1934.

Yes

No

If "Yes" is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): 82-\_\_\_\_

This Report on Form 6-K with respect to our Interim Financial Statements and Notes thereon for the six-month period ended June 31, 2006, other than page 149 thereof, is hereby incorporated by reference in the following HSBC Holdings plc registration statements: file numbers 333-10474, 333-92024, 333-102027, 333-103887, 333-104203, 333-109288, 333-113427, 333-127327, 333-126531 and 333-135007.

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HSBC HOLDINGS PLC

**Interim Report 2007**

Headquartered in London, HSBC is one of the largest banking and financial services organisations in the world. Its international network comprises over 10,000 properties in 83 countries and territories in Europe; Hong Kong; Rest of Asia-Pacific, including the Middle East and Africa; North America and Latin America.

With listings on the London, Hong Kong, New York, Paris and Bermuda stock exchanges, shares in HSBC Holdings plc are held by about 200,000 shareholders in over 100 countries and territories. The shares are traded on the New York Stock Exchange in the form of American Depositary Shares.

HSBC provides a comprehensive range of financial services to more than 125 million customers through four customer groups and global businesses: Personal Financial Services (including consumer finance); Commercial Banking; Corporate, Investment Banking and Markets; and Private Banking.

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<sup>1</sup> Supplementary contents are provided on the referenced pages.

## **Certain defined terms**

Unless the context requires otherwise, **HSBC Holdings** means HSBC Holdings plc and **HSBC** means HSBC Holdings together with its subsidiaries. Within this document, the Hong Kong Special Administrative Region of the People's Republic of China is referred to as **Hong Kong**. When used in the terms **shareholders' equity** and **total shareholders' equity**, **shareholders** means holders of HSBC Holdings ordinary and preference shares classified as equity.

*The Interim Report 2007 of HSBC Holdings has been prepared in accordance with the requirements of English law, and liability in respect thereof is also governed by English law. In particular, the liability of the Directors for these reports is solely to HSBC Holdings. HSBC's interim Financial Statements and Notes thereon, as set out on pages 132 to 155, have been prepared in accordance with International Accounting Standard (IAS) 34 Interim Financial Reporting. HSBC prepares its annual consolidated financial statements in accordance with International Financial Reporting Standards (IFRSs) as endorsed by the European Union (EU). At 30 June 2007, there is no difference between IFRSs as endorsed by the EU and IFRSs as issued by the International Accounting Standards Board (IASB) in terms of their application by HSBC.*

*HSBC uses the US dollar as its presentation currency because the US dollar and currencies linked to it form the major currency bloc in which HSBC transacts its business. Unless otherwise stated, all figures are presented in this document on a consolidated basis.*

*When reference is made to underlying or underlying basis in tables or commentaries, comparative information has been expressed at constant currency (see page 3) and adjusted for the effects of acquisitions and disposals.*

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HSBC HOLDINGS PLC

## Financial Highlights

### For the half-year

- Total operating income up 23 per cent to US\$42,092 million (US\$34,334 million in the first half of 2006).
- Group pre-tax profit up 13 per cent to US\$14,159 million (US\$12,517 million in the first half of 2006).
- Profit attributable to shareholders of the parent company up 25 per cent to US\$10,895 million (US\$8,729 million in the first half of 2006).
- Return on average invested capital of 18.4 per cent (17.2 per cent in the first half of 2006).
- Earnings per share up 22 per cent to US\$0.95 (US\$0.78 in the first half of 2006).

### Dividends and capital position

- Tier 1 capital ratio of 9.3 per cent and total capital ratio of 13.2 per cent.
- Second interim dividend for 2007 of US\$0.17 per share which, together with the first interim dividend for 2007 of US\$0.17 per share already paid, represents an increase of 13 per cent over the first and second interim dividends for 2006.

### Cautionary statement regarding forward-looking statements

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This *Interim Report 2007* contains certain forward-looking statements with respect to the financial condition, results of operations and business of HSBC. These forward-looking statements represent HSBC's expectations or beliefs concerning future events and involve known and unknown risks and uncertainty that could cause actual results, performance or events to differ materially from those expressed or implied in such statements. For example, certain of the market risk disclosures, some of which are only estimates and, therefore, could be materially different from actual results, are dependent on key model characteristics and assumptions and are subject to various limitations. Certain statements, such as those that include the words potential, value at risk, estimated, expects, anticipates, objective, intends, plans, believes, estim, expressions or variations on such expressions may be considered forward-looking statements.

Written and/or oral forward-looking statements may also be made in the periodic reports to the US Securities and Exchange Commission (SEC) on Form 20-F, Form 6-K, summary financial statements to shareholders, proxy statements, offering circulars and prospectuses, press releases and other written materials and in oral statements made by HSBC's Directors, officers or employees to third parties, including financial analysts.

Forward-looking statements involve inherent risks and uncertainties. Readers should be cautioned that a number of factors could cause actual results to differ, in some instances materially, from those anticipated or implied in any forward-looking statement. Forward-looking statements speak only as of the date they are made, and it should not be assumed that they have been reviewed or updated in the light of new information or future events. Trends and factors that are expected to affect HSBC's results of operations are described in the Business Review, the Financial Review, and The Management of Risk. A more detailed cautionary statement is given on pages 4 and 5 of *Annual Report and Accounts 2006*.



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**Financial Highlights** (continued)**Profitability and balance sheet data**

|   | Half-year to             |                          |                              |
|---|--------------------------|--------------------------|------------------------------|
|   | 30 June<br>2007<br>US\$m | 30 June<br>2006<br>US\$m | 31 December<br>2006<br>US\$m |
| <b>For the period</b>   |                          |                          |                              |
| Total operating income  | 42,092                   | 34,334                   | 35,736                       |
| Profit before tax   | 14,159                   | 12,517                   | 9,569                        |
| Profit attributable to shareholders of the parent company                               | 10,895                   | 8,729                    | 7,060                        |
| Dividends   | (6,192)                  | (5,270)                  | (3,499)                      |
| <b>At the period-end</b>  |                          |                          |                              |
| Total equity  | 126,491                  | 107,370                  | 114,928                      |
| Total shareholders' equity  | 119,780                  | 101,381                  | 108,352                      |
| Capital resources <sup>1</sup>  | 137,042                  | 116,636                  | 127,074                      |
| Customer accounts   | 980,832                  | 833,742                  | 896,834                      |
| Total assets  | 2,150,441                | 1,738,138                | 1,860,758                    |
| Risk-weighted assets  | 1,041,540                | 872,893                  | 938,678                      |
|   | US\$                     | US\$                     | US\$                         |
| <b>Per ordinary share</b>   |                          |                          |                              |
| Basic earnings  | 0.95                     | 0.78                     | 0.62                         |
| Diluted earnings  | 0.94                     | 0.77                     | 0.62                         |
| Dividends   | 0.53                     | 0.46                     | 0.30                         |
| Net asset value at period end   | 10.10                    | 8.71                     | 9.24                         |
| <b>Capital and performance ratios (annualised)</b>                                      |                          |                          |                              |
|   | %                        | %                        | %                            |
| <b>Capital ratios</b>   |                          |                          |                              |
| Tier 1 capital  | 9.3                      | 9.4                      | 9.4                          |
| Total capital   | 13.2                     | 13.4                     | 13.5                         |
| <b>Performance ratios</b>   |                          |                          |                              |
| Return on average invested capital <sup>2</sup>   | 18.4                     | 17.2                     | 12.8                         |
| Return on average total shareholders' equity <sup>3</sup>                               | 19.1                     | 18.1                     | 13.4                         |
| Post-tax return on average total assets   | 1.19                     | 1.12                     | 0.88                         |
| Post-tax return on average risk-weighted assets   | 2.30                     | 2.21                     | 1.65                         |
| <b>Credit coverage ratios</b>   |                          |                          |                              |
| Loan impairment charges as a percentage of total operating income                       | 15.0                     | 11.3                     | 18.6                         |
| Loan impairment charges as a percentage of average gross customer advances              | 1.53                     | 1.04                     | 1.73                         |
| Total impairment allowances outstanding as a percentage of impaired loans at period end | 98.4                     | 92.5                     | 98.5                         |
| <b>Efficiency and revenue mix ratios</b>  |                          |                          |                              |
| Cost efficiency ratio <sup>4</sup>  | 48.3                     | 50.1                     | 52.5                         |

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As a percentage of total operating income:

|                     |      |      |      |
|---------------------|------|------|------|
| net interest income | 43.3 | 48.7 | 49.7 |
| net fee income      | 24.9 | 24.4 | 24.6 |
| net trading income  | 13.1 | 12.4 | 11.1 |

### Financial ratio

|  |     |     |     |
|--|-----|-----|-----|
| Average total shareholders' equity to average total assets | 5.9 | 5.9 | 6.1 |
|--|-----|-----|-----|

- 1 *Capital resources are total regulatory capital, the calculation of which is set out on page 127.*
- 2 *The definition of return on average invested capital and a reconciliation to the equivalent Generally Accepted Accounting Principles ( GAAP ) measures are set out on page 92.*
- 3 *The return on average total shareholders' equity is defined as profit attributable to shareholders of the parent company divided by average total shareholders equity.*
- 4 *The cost efficiency ratio is defined as total operating expenses divided by net operating income before loan impairment charges and other credit risk provisions.*

[Back to Contents](#)**Share information**

|   | At<br>30 June<br>2007 | At<br>30 June<br>2006   | At<br>31<br>December<br>2006 |
|---|-----------------------|-------------------------|------------------------------|
| US\$0.50 ordinary shares in issue (million)                             | 11,713                | 11,481                  | 11,572                       |
| Market capitalisation (billion)   | US\$215               | US\$202                 | US\$212                      |
| Closing market price per ordinary share:                                |                       |                         |                              |
| London  | £9.15                 | £9.52                   | £9.31                        |
| Hong Kong   | HK\$142.50            | HK\$136.10              | HK\$142.40                   |
| Closing market price per American Depositary Share ( ADS <sup>1</sup> ) | US\$91.77             | US\$88.35               | US\$91.65                    |
|   | <b>Over 1 year</b>    | <b>Over 3<br/>years</b> | <b>Over 5<br/>years</b>      |
| HSBC total shareholder return to 30 June 2007 <sup>2</sup>              | 101.2                 | 129.1                   | 156.6                        |
| Benchmarks:   |                       |                         |                              |
| FTSE 100 <sup>3</sup>   | 117.1                 | 163.8                   | 168.5                        |
| MSCI World <sup>4</sup>   | 124.2                 | 161.4                   | 197.2                        |

1 Each ADS represents five ordinary shares.

2 Total shareholder return is defined on page 282 of the Annual Report and Accounts 2006.

3 The Financial Times-Stock Exchange 100 Index.

4 The Morgan Stanley Capital International World Index.

**Constant currency**

Constant currency comparatives for the half-years to 30 June 2006 and 31 December 2006, used in the 2007 commentaries, are computed by retranslating into US dollars:

- the income statements for the half-years to 30 June 2006 and 31 December 2006 of non-US dollar branches, subsidiaries, joint ventures and associates at the average rates of exchange for the half-year to 30 June 2007; and
- the balance sheets at 30 June 2006 and 31 December 2006 for non-US dollar branches, subsidiaries, joint ventures and associates at the rates of exchange ruling at 30 June 2007.

No adjustment has been made to the exchange rates used to translate foreign currency denominated assets and liabilities into the functional currencies of any HSBC branches, subsidiaries, joint ventures or associates.

When reference is made to constant currency or constant exchange rates in tables or commentaries, comparative data reported in the functional currencies of HSBC's operations have been translated at the appropriate exchange rates applied in the current period on the basis described above.

**Growth in operating income and costs**

Half-year to 30 June 2007 compared with the half-year  
to

| 30 June 2006 |  | 31 December 2006 |  |
|--------------|--|------------------|--|
| As reported  | Constant<br>currency<br>on an<br>underlying<br>basis | As reported      | Constant<br>currency<br>on an<br>underlying<br>basis |
| %            | %  | %                | %  |
|              |  |                  |  |



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|  |    |    |    |    |
|--|----|----|----|----|
| Growth in net operating income before loan impairment charges and other credit risk provisions | 20 | 15 | 16 | 13 |
| Growth in total operating expenses   | 15 | 10 | 7  | 4  |

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HSBC HOLDINGS PLC

## Group Chairman's Statement

HSBC produced record results for the first half of 2007, delivering profit before tax of US\$14.2 billion, up 13 per cent, and earnings per share of US\$0.95, up 22 per cent.

The Directors have approved a second interim dividend of US\$0.17 per share, which will be payable on 4 October 2007 with a scrip alternative, in accordance with our planned schedule of quarterly dividends.

The results were driven by excellent performances across Asia, and in Corporate, Investment Banking and Markets (CIBM) and Commercial Banking, which offset the impact of higher consumer finance impairment charges in the US and a challenging environment for our Personal Financial Services business in Europe.

Our results benefited from two specific items. First, we recognised a gain of US\$1 billion in attributable profit, as a result of the dilution of our holdings in our mainland China associates. Excluding this exceptional gain, profit before tax rose by 5 per cent and attributable profit by 13 per cent. Second, our effective tax rate was unusually low at 18.7 per cent in this period. The following comments exclude the impact of the dilution gain.

Revenues grew by US\$5.2 billion, or 16 per cent, against cost growth of US\$2.5 billion, or 15 per cent, contributing to an improved cost-efficiency ratio of 49.7 per cent.

Asia drove profit growth, with Hong Kong ahead by 25 per cent and Rest of Asia-Pacific by 37 per cent. Latin America and Europe delivered results ahead of the prior year period by 16 per cent and 13 per cent, respectively. As expected, North

America was lower by 35 per cent as a consequence of higher impairment reserves. It is worth noting that our results for the first half of 2006 benefited from exceptionally low impairment charges in the US as a result of changes in US bankruptcy law.

At a customer group level, Commercial Banking delivered pre-tax profits 20 per cent ahead of last year, and both CIBM and Private Banking were at least 30 per cent ahead. Our Personal Financial Services businesses in Asia also delivered very strong results, with pre-tax profits 38 per cent ahead of the interim stage last year. However, pre-tax profits in Personal Financial Services as a whole declined by 20 per cent overall compared with the first half of 2006, owing to challenging conditions in the UK and to the weaknesses we have already highlighted in our US correspondent mortgage business. The actions taken to restructure and manage down our exposure in this business are progressing well. The charge for impairments was lower than in the second half of last year and, importantly, was in line with our expectations.

Within these results, the Group's Insurance operations made a significant contribution and we see insurance as a growth opportunity for the future.

From a strategic perspective, these results illustrate the value we are creating from our position as the world's largest and most profitable international emerging markets bank, and from our unique global reach which allows us to act as a bridge between developed and developing markets for our customers.

The strong growth we achieved in operating revenues reflects our focus on seeking out growth markets and has allowed us to continue to invest in organic expansion while maintaining a strong capital position and growing dividends to shareholders.

Average invested capital rose by US\$17 billion as we pursued expansion opportunities around the world. Our tier one capital ratio remained strong at 9.3 per cent. We see this as a competitive advantage, particularly in the current economic environment, and in light of the opportunities we see to deploy this capital within our businesses.

In an increasingly globalised world, the success we have reported today is supported by the integrity that is part of our global brand, and which we believe constitutes a distinct competitive advantage. In less than a decade, we have made HSBC the 23rd most valuable brand in the world, according to Interbrand, and we are the fastest growing financial services brand. We will continue to invest in developing our brand and the

experience it promises

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for the customers and communities we serve around the world. We will also extend our brand to new markets and new business streams.

As I set out earlier this year, we are refocusing our business to make the most of the opportunities presented by three major trends that are reshaping the world economy. First, emerging markets are growing faster than mature economies. Second, world trade is growing significantly faster than world GDP. Third, longevity is increasing around the world.

As a result, we have positioned our business so that it is broadly balanced between Asia, Latin America, the Middle East and other developing economies, and slower-growing developed economies. As the world economy evolves, and trade and investment flows from and into emerging markets expand, HSBC has an excellent platform for growth. It is the linkages between our business operations across 83 countries and territories which deliver unique revenue opportunities and a distinctive competitive position. Increasing longevity is also creating opportunities to grow our insurance and retirement businesses. All these factors contributed to the growth we delivered in the first half of 2007.

I want to thank all my colleagues for their contribution to these results. Our progress is clear evidence of the value we are delivering through our strategy of joining up the company for our customers, our shareholders and our people.

As the world's local bank, our responsibilities extend beyond how successfully we run our business. Climate change is one of the most significant issues of our time, which is why we announced in May the US\$100 million HSBC Climate Partnership, working with four world-class organisations to support initiatives by individuals, businesses and governments around the world to address this issue. I am also delighted that Sir Nicholas Stern – author of the *Stern Report* on the economics of climate change – has agreed to become an adviser on economic development and climate change to HSBC.

## Outlook

The world economy remains remarkably buoyant. There is growing evidence of economic decoupling, with US weakness not constraining economic activity elsewhere. Even in the US, which faces considerable housing and sub-prime-related difficulties, consumer spending has remained encouragingly robust and the labour market has been firm. The financial markets continue to enjoy record

levels of activity, though muted in the past couple of months by nervousness about credit markets, and more sophisticated product structuring and risk management services are enabling the diversification and spread of risk on an unprecedented scale. This buoyancy is supporting economic activity.

We estimate that global growth this year will be close to last year's 3.8 per cent. We believe emerging markets will remain particularly strong, stimulating global demand for capital goods, providing an economic boost to Germany, Japan and other major exporters. The weakness in the housing market is likely to hold back US growth for 2007, which may be as low as 2 per cent.

There are risks, however. Excess liquidity in global financial markets could lead to further asset price dislocation. Perceptions of risk can change very rapidly, affecting both credit spreads and liquidity, and history shows that when market participants simultaneously seek to adjust risk exposures, market instability can follow. Among the potential triggers are higher global interest rates with a return to higher inflation, moves towards protectionism and greater spillover effects from US housing market weakness. HSBC has always emphasised balance sheet strength to maintain strong liquidity and a sound capital base to take advantage of opportunities that arise in such circumstances. We remain cautious in our risk appetite.

Our strategy is clear. We have well diversified earnings by both geography and customer. Our distribution network provides compelling opportunities for serving our customers around the world. We will continue to improve both customer experience and operating efficiency through technology, especially in our direct channels. The outlook for HSBC is buoyed by our expectation of continuing strong growth in our developing markets businesses and their greater linkages internationally. We are on a journey with great opportunities to build on our strong current position, and I look forward to reporting our future progress.

Stephen Green, *Group Chairman*

30 July 2007



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HSBC HOLDINGS PLC

## Group Chief Executive's Review

Our first half results demonstrate sustainable growth and significant progress in working through the challenges of sub-prime lending, whilst also unlocking real value from our world-class distribution network through Joining up the company .

### The world's largest and most profitable international emerging markets bank

Our emerging markets operations continue to perform exceptionally well. We prioritise investment in growing these businesses organically and we continue to extract value from strategic investments. This month our integration of Grupo Banistmo continued as we rebranded operations to HSBC in five Latin American countries.

We have a strong presence in the world's most dynamic economies. In the BRIC countries – forecast to account for 40 per cent of world growth by 2025 – we are the largest international bank in mainland China, the second largest and growing impressively in India, and the third largest in Brazil. In Russia, we received a banking licence in May to start retail banking activities.

### Joining up the company for our customers

The breadth of our international network means we can offer our customers compelling global propositions that cannot be matched by purely domestic or regional competitors. Increasingly, we are joining up our businesses for our customers across borders and across businesses. Our Corporate, Investment Banking and Markets ( CIBM ) business achieved record results for the period by successfully

executing its emerging markets-led and financing-focused strategy. Our Commercial Banking business also grew strongly as customers benefited from our international orientation and the direct channels we are building for them.

Personal Financial Services' profit before tax declined by 20 per cent, largely as a consequence of our experience with sub-prime correspondent mortgages in the US and weakness in the UK. Meanwhile in Asia, pre-tax profit grew by 38 per cent.

We are increasingly connecting this business globally and in May rolled-out in 35 countries our market-leading Premier proposition – a signature account for international HSBC Premier customers. First indications are encouraging and there is an opportunity to gain significant global market share in this valuable segment. We believe that, over time, we will add four million new mass-affluent customers.

Private Banking achieved very strong results and continued to leverage closer links with other customer groups, particularly Commercial Banking, generating almost US\$2 billion in total client assets from referrals. When our investment business recently launched the first multi-manager Chinese equity fund in Hong Kong, we were able to raise over US\$1 billion from our retail and private banking customer base in the region.

We also benefit from the ability to deliver global world-class propositions for our customers through the effective use of our technology. By building core systems for use across the Group, we can share the development and support costs across our operations, close down old systems, and share best practice in sales and service.

In our cards business, the introduction of our Whirl global credit card platform across the world, which now services 86 million accounts across 16 countries, has allowed us to improve services for our card customers and to cut our IT costs per account by 16 per cent. We are adding 40,000 credit card customers to the system each day.

We are also introducing a new personal and business internet platform across the Group. This has been implemented in 25 countries so far. Internet sales have risen 68 per cent compared to the first half of 2006. The new infrastructure is allowing us to launch new services, including direct banking. Following earlier successes in the US and Taiwan, HSBC Direct, our online direct banking and savings proposition, was launched in South Korea and Canada during the first half of 2007. In Asia, the



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service has attracted over 120,000 customers, with total savings balances exceeding US\$900 million. The US business has continued to perform strongly; online savings balances have now reached US\$12 billion with over 225,000 new accounts added this year. One of the compelling features of the HSBC Direct model is that it allows us to attract new customers who we do not reach through our existing channels. We continue to develop the HSBC Direct model, with a view to rolling it out in other markets.

In Latin America, we are introducing HSBC's systems into the newly acquired Grupo Banistmo companies, starting with Panama. We are also implementing HSBCnet throughout Latin America to provide a full cash management system across the region.

### **Number one international bank in Asia**

We produced record results in Asia. Profit before tax grew impressively in all our major markets, with our operations in Hong Kong up by 25 per cent, our businesses in mainland China by 69 per cent, in India by 39 per cent, in Indonesia by 115 per cent, in Malaysia by 13 per cent and in Singapore by 44 per cent.

Hong Kong produced very strong results. As a result of its leading position in wealth management, our business there was well-positioned to benefit from the buoyant stock market activity during the period and the steady flow of mainland China companies listing on the Hong Kong Stock Exchange. We also continued to leverage our position as the leading financial institution in Hong Kong in trade finance and in insurance. Increased foreign investment through Hong Kong into mainland China boosted Hong Kong's services and property sectors, and provided further opportunities for HSBC to generate revenue growth.

Strong domestic interest in stock market investments within mainland China also encouraged listings on the Shanghai Stock Exchange during this period, and our three associates, Bank of Communications, Ping An Insurance and Industrial Bank, all successfully raised new capital. The resulting dilution of our interests was considerably less than our share of the new monies raised, and our results reflect aggregate gains at the attributable profit level of some US\$1 billion, or US\$0.09 per share, which should be regarded as exceptional.

We reinforced HSBC's position as the leading international bank in mainland China. Our domestic operations in mainland China, following local incorporation, grew strongly, with deposit and asset

growth of over 50 per cent and 26 per cent respectively, compared with the same period last year. Pre-tax profits grew by 69 per cent to US\$473 million. We added seven outlets to what is already the largest international branch network and recruited over 800 new staff to support business growth.

In India, strong performance in CIBM drove the 39 per cent rise in profit before tax. We significantly expanded our customer base and continued to invest heavily in growing our business organically, particularly in consumer finance, while maintaining a largely unchanged cost efficiency ratio at 55 per cent.

In Indonesia, where we are also investing in developing our consumer finance business and opened 20 new outlets in the period, profit before tax grew 115 per cent to US\$58 million. In Vietnam, a market with great long-term potential, we agreed to increase our stake in Techcombank and we are also growing our own business rapidly there. We grew profit before tax by 117 per cent to US\$21 million in the first half, and increased headcount by a third.

Across Asia as a whole, our Commercial Banking business performed very well, thanks in part to our success in growing the customer base. Commercial Banking customers in Asia have increased by 6 per cent in the past year, with particularly strong growth in mainland China and South Korea.

Our success in Asia is being driven in large part by our success in joining up the Group to leverage skills transfer and international reach. In particular, in our investment business, our Asian operations are capturing the leading share of securities services revenues from custody and administration for international funds groups. Reciprocally, we are producing developing market products, both for our own asset management group and for third parties to distribute in the developed world. Similar linkages exist in capital markets activities, remittance services, cross-referral of commercial customers transacting overseas and in consumer finance expansion throughout Asia.

### **Integration and development in Latin America on track**

Profit before tax for Latin America grew by 16 per cent. From a handful of offices a decade ago to some 4,000 in the region today, our operations now account for 8 per cent of Group profit. We are one of the largest international banks in the region, and we continue to develop our businesses in our major





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HSBC HOLDINGS PLC

## Group Chief Executive's Review (continued)

markets in Mexico, Brazil, Argentina and now across Central America. This was the first complete half-year contribution from Grupo Banistmo, the leading bank in Central America, following its acquisition in 2006. Pre-tax contribution of US\$49 million was in line with our expectations and integration is proceeding well.

Improved credit performance in Brazil, coupled with strong asset growth, contributed to a rise in pre-tax profit of 43 per cent. Growth in secured lending and invoice financing has set the scene for sustained revenue growth, and insurance sales in the existing customer base were also stronger.

Revenue growth in Mexico remained strong at just over 23 per cent as we improved market share. We have built a highly successful business in the last five years, which has already returned profits in excess of our total investment. In the first half of 2007, customer acquisition grew at a higher rate than forecast, and related costs affected profits through a rise in provisions which largely offset the expansion in revenues. HSBC in Mexico continued to build market share with credit cards, *Tu Cuenta* packaged accounts and Premier accounts all growing by over 45 per cent compared with the previous year.

In Argentina, the successful integration of Banca Nazionale del Lavoro, a well-timed acquisition in May 2006, contributed to a 14 per cent rise in pre-tax profits to US\$95 million. Once again CIBM, working with local management, helped HSBC in Argentina maintain leading positions in foreign exchange and trade services for multinational companies operating there.

### Benefiting from organic growth in the Middle East

Our Middle East businesses, excluding Saudi Arabia, grew strongly, with profit before tax up by 31 per cent. Our operations in the United Arab Emirates and in Egypt performed well as the region expanded its infrastructure development and its outward investment, supported by sustained high oil prices.

Commercial Banking enjoyed higher revenues as a result of the region's high growth and increased trade flows. High liquidity in the region and demand from institutional customers led to strong sales of structured derivatives and other products in CIBM.

The rollout of additional branches and customer service units, the expansion of the direct sales force and sales of Premier products drove increased personal customer numbers and higher revenues.

The contribution from Saudi Arabia was, however, lower as the stock market declines which

occurred in the second half of last year dampened market activity in the first half of 2007.

### Europe: investing in emerging markets and strong returns from UK Commercial Banking

Within emerging Europe, profits in Turkey grew by 34 per cent, even as we opened 25 new branches and installed 101 ATMs to develop our retail platform. Further expansion is planned for the second half of the year. We obtained a licence to begin retail business in Russia, where we aim to open over 35 branches in the next three years.

We intend to expand our operations in Poland, the Czech Republic and Slovakia for personal customers, and we are looking at other markets in Central and Eastern Europe. We will also be opening more branches in Armenia, expanding in Kazakhstan, and we have applied for a licence to begin operations in Georgia.

In continental Europe, our French operations were strongly ahead of the comparable prior period, with profits growing by US\$219 million, driven by CIBM revenue growth.

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UK Commercial Banking continued to perform well. Profit before tax rose by 18 per cent, our customer base expanded, and we are now the bank most recommended by our start-up customers. Investment in technology is improving customer service and productivity; the successful positioning of Business Direct has attracted over 40,000 customers since its launch in September 2006, of which 60 per cent are new to the Group.

Our Personal Financial Services business in Europe was, however, 34 per cent down on the comparable period in 2006. This was largely due to two factors. First, a deliberate reduction in credit exposure to sectors whose pricing, in our view, inadequately reflects risk. Second, the impact in the UK of unauthorised overdraft fee refunds, which increased our costs by US\$236 million. This is an industry-wide issue and the size of the refunds that we have made demonstrates our commitment to treating our customers in a fair and transparent manner. Indeed, we very much welcome the agreement with the Office of Fair Trading to take the case to court to achieve legal clarity and a resolution for our customers and our business. In Group terms, our Personal Financial Services business in the UK typically represents less than 7 per cent of our worldwide profits.

Nevertheless, this remains a highly challenging operating environment. We continue to focus on customer acquisition and retention, and we see

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growth opportunities in wealth management and insurance to counterbalance the challenges posed by competition and regulation for current account pricing.

We grew strongly in packaged fee-based accounts, in Premier accounts, and in retail savings products, which helped to offset the reduction in lending margin. Average savings balances increased by 14 per cent in the first half to US\$83 billion. In First Direct we have the UK's most recommended bank for every one of the 15 years the measure has existed and we will learn from its expertise as we build direct channels around the world.

**Good progress in managing down the mortgage services portfolio in North America**

Within North America, our Canadian and Bermudian businesses grew pre-tax profits by 22 per cent and, although our US businesses were 43 per cent below the pre-tax performance achieved in the first half of 2006, they recovered strongly against the second half of last year, delivering pre-tax profits of US\$1.8 billion – an improvement of US\$1.5 billion.

This recovery in profitability reflected the success of the steps we have taken to manage loss exposure within the correspondent channel mortgage business. There was no significant change to the levels of loan impairment reserves established at the end of last year. Credit impairment charges in mortgage services in the half year were US\$760 million and we wrote off loans of US\$715 million against allowances already raised. As a result our impairment allowances remained largely unchanged at US\$2.1 billion. We have stopped underwriting sub-prime mortgages within the mortgage services correspondent business, centralised collection activities at one centre for the most at-risk customers, made management changes in key accountabilities, and put in place a proactive calling programme to reach out to customers facing interest rate resets in the coming months. In contrast to many lenders, we are able to manage these relationships directly because we own the loan and the servicing. This means that we can have a more positive dialogue with customers and can actively manage our portfolio in this challenging environment. Since we started the contact programme at the end of 2006, we have contacted 19,000 customers, and have modified the loans for over 5,000 of them, benefiting both our customers and our business.

With the benefit of a resilient US economy, we have managed down the mortgage services exposure

to US\$41.4 billion, a reduction of some US\$8 billion from the beginning of the year, a trend we hope to continue in the second half. We have also managed down the value of resets in the mortgage services portfolio due in the second half by almost a quarter to US\$5.3 billion.

The remaining US consumer finance businesses continued to meet expectations, led by branch-based consumer lending. There is growing evidence that the reduction of capacity in the sub-prime mortgage industry, coupled with curtailment of most of the structured affordability products offered, is leading to more disciplined underwriting and pricing across the industry. This is reducing acquisition costs and improving customer retention. As a result, our US consumer finance revenues were 2 per cent and 5 per cent higher compared with the first and second halves of 2006, respectively.

In our US retail bank, we continued to expand beyond residential mortgage lending. We are growing our branch network in California, Connecticut, New Jersey, Florida and the Metro DC Area, and continuing to roll out HSBC Direct, our highly successful online business.

**Record results in CIBM reflecting focus on emerging markets and financing**

Our strategy of positioning our CIBM business as emerging markets-led and financing-focused is paying off, with profits growing by 32 per cent to a new high of US\$4 billion. Asian (including Middle Eastern) and Latin American operations contributed 49 per cent of CIBM's pre-tax profits in the first half of 2007.

In Asia, success in financing and providing structuring and hedging solutions for the growing investment flows into and from the region, together with growth in traditional foreign exchange and securities activities, delivered an additional US\$479 million of pre-tax profits, a rise of 36 per cent. Europe also achieved strong growth as CIBM's product hubs in London and Paris delivered a full spectrum of products both within Europe and to the global HSBC network.

Especially encouraging was the growing number of notable mandates in sizeable cross-border financing transactions which leveraged HSBC's presence in both countries. These included: Saudi Basic Industries Corp.'s US\$11.6 billion acquisition of GE Plastics; Singapore Telecommunications Ltd.'s US\$758 million acquisition of 30 per cent of Warid Telecom (Pvt) Ltd. of Pakistan; National Titanium Dioxide Co. of Saudi Arabia's US\$1.2 billion acquisition of Lyondell Chemical



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HSBC HOLDINGS PLC

## Group Chief Executive's Review (continued)

Co.'s inorganic chemicals business in the US; and Dubai Drydocks' S\$650 million acquisition of Pan-United Marine Ltd. of Singapore.

HSBC also acted as lead arranger of financing facilities for Macquarie of £1.8 billion for the acquisition of O2 Airwave and £3.4 billion for the acquisition of National Grid Wireless.

We were pleased to be recognised in industry awards: HSBC was named global Best Risk Management House in *the Economist* magazine 2007 Awards for Excellence. We also won global Best Cash Management House in *the Economist* awards. In debt capital markets, HSBC ranked first in the Asian local currency Bloomberg bond league table, first in the sterling bond league table and sixth in the international bond league table.

### Developing our income stream in Insurance

Less than 15 per cent of HSBC customers currently take an insurance product from us. Our insurance operations across our customer groups are making an important contribution to the Group and we believe that insurance has the potential over time to represent a fifth of Group pre-tax profits.

We have started our work towards this by strengthening the management team and launching the HSBC Insurance brand, repositioning for growth and aiming to be a top-10 player. We are committed to the life, pensions and investments business and to working with preferred strategic partners in general insurance, and to raising the Group's retention levels.

We announced three insurance deals in three months. In France, where we are building our life, pensions, investments and retirement services business, we acquired the remaining 50 per cent of Erisa, the life, property and casualty insurer, from our former joint venture partner, Swiss Life, for a consideration of 229 million. In the UK, HSBC Bank plans to partner with Aviva to create a joint venture under the HSBC Insurance brand. In India, we plan to create a joint venture life insurance company Canara HSBC Life Insurance with Canara Bank and the Oriental Bank of Commerce. The new company will have access to the customers of both banks – 40 million people in total – and provides a platform for growth in India's expanding life insurance market.

### Global wealth creation supporting strong growth in private banking

Given the strong economic background and buoyant property and stock markets in many parts of the

world, increasing wealth accumulation drove strong growth in client assets and sales of structured investment products within our private banking operations. Client assets grew by 11 per cent to reach US\$370 billion. Fee revenues within the private bank were up by 15 per cent to a record US\$811 million. In part, this reflected improved cooperation between our commercial bank and the private bank in terms of customer referral, and the use of our in-house structuring capabilities in CIBM to build the products demanded by the private bank's customers.

### Global credit environment

Apart from US sub-prime mortgages, the credit environment generally remained favourable globally in the first half of the year, with continuing low levels of impairment emerging across our corporate and commercial lending books. Encouragingly, more recent underwriting of unsecured personal lending in the UK has performed better, although credit impairment has remained at the elevated levels experienced in the past two years.

High levels of liquidity and demand for higher yielding debt, combined with investor appetite for higher leverage, have historically supported the restructuring of corporate balance sheets. We remain alert, however, to the probability of a change in sentiment, in particular as risk premia are rising and interest rates move on an upward trend across much of the world.

### A clear way forward

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The management team has a clear strategy to execute and we have produced strong results for the half-year. We will build on these results during the rest of the year. We are focused on growing revenues by joining up the company for the benefit of our customers. We are intent on slowing cost growth by using technology to re-engineer our processes in a meaningful way. We believe there is great potential to unlock further value from HSBC and we aim to do precisely that.

Michael Geoghegan, *Group Chief Executive*

30 July 2007

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HSBC HOLDINGS PLC

**Business Review**

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**Principal activities**

HSBC is one of the largest banking and financial services organisations in the world, with a market capitalisation of US\$215 billion at 30 June 2007.

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 over 10,000 properties in 83 countries and territories in five geographical regions: Europe; Hong Kong; Rest of Asia-Pacific, including the Middle East and Africa; 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 consumer finance operations.

**Strategic direction**

HSBC's strategic direction is to be the world's leading financial services company, with 'leading' meaning the HSBC brand is preferred to others and HSBC's corporate character is admired, its earnings per share growth is dynamic and it holds leadership positions in selected markets. Financial success is measured in terms of earnings growth and by comparing the Group's total shareholder return (TSR) target against a weighted TSR benchmark composed of a peer group of banks.

To achieve its strategy, the Group has identified seven priorities or 'global pillars' that will guide the Group's strategic initiatives in 2007 and 2008. Success in achieving the priorities will be assessed by reviewing a suite of key performance indicators. The global pillars are:

- to exploit HSBC's global reach by more effectively joining up the company by country, distribution channel, customer group and global business;
- to improve its customer experience so that customers feel that HSBC is the best place to bank;



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- to invest in developing HSBC's brand and to encourage all staff to live HSBC's brand values in their day-to-day activities;
- to improve staff engagement by ensuring employment policies are progressive, perceptive, responsive, respectful and fair;
- to grow the business by focusing on deposit-taking and achieving the right balance between risk and reward;
- to enhance working practices and use technology more effectively to make it easier for customers to do business with the Group; and
- to clearly allocate responsibility for delivery of the above initiatives to country managers and heads of customer groups and global businesses, with Group Head Office and regional head offices providing guidance and, where appropriate, delegating authority.

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HSBC HOLDINGS PLC

**Business Review** (continued)**Customer groups and global businesses****Summary**

HSBC manages its business through two customer groups, Personal Financial Services and Commercial Banking, and two global businesses, Corporate, Investment Banking and Markets ( CIBM ), and

Private Banking. Personal Financial Services incorporates the Group's consumer finance businesses, reflecting their increasing integration within mainstream financial services around the world. The largest of these is HSBC Finance Corporation ( HSBC Finance ), one of the leading consumer finance companies in the US.

## Profit before tax

|   | Half-year to  |              |               |              |                  |              |
|---|---------------|--------------|---------------|--------------|------------------|--------------|
|   | 30 June 2007  |              | 30 June 2006  |              | 31 December 2006 |              |
|   | US\$m         | %            | US\$m         | %            | US\$m            | %            |
| Personal Financial Services               | 4,729         | 33.4         | 5,908         | 47.2         | 3,549            | 37.1         |
| Commercial Banking                        | 3,422         | 24.2         | 2,862         | 22.9         | 3,135            | 32.8         |
| Corporate, Investment Banking and Markets | 4,158         | 29.4         | 3,144         | 25.1         | 2,662            | 27.8         |
| Private Banking                           | 780           | 5.5          | 600           | 4.8          | 614              | 6.4          |
| Other                                     | 1,070         | 7.5          | 3             |              | (391)            | (4.1)        |
|   | <b>14,159</b> | <b>100.0</b> | <b>12,517</b> | <b>100.0</b> | <b>9,569</b>     | <b>100.0</b> |

Total assets<sup>1</sup>

|   | At 30 June 2007 |      | At 30 June 2006 |      | At 31 December 2006 |      |
|---|-----------------|------|-----------------|------|---------------------|------|
|   | US\$m           | %    | US\$m           | %    | US\$m               | %    |
| Personal Financial Services               | 577,402         | 26.9 | 511,552         | 29.4 | 546,568             | 29.4 |
| Commercial Banking                        | 225,763         | 10.5 | 186,195         | 10.7 | 213,450             | 11.5 |
| Corporate, Investment Banking and Markets | 1,220,316       | 56.7 | 940,177         | 54.1 | 994,436             | 53.4 |
| Private Banking                           | 81,916          | 3.8  | 67,643          | 3.9  | 73,026              | 3.9  |
| Other                                     | 45,044          | 2.1  | 32,571          | 1.9  | 33,278              | 1.8  |

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|                  |              |           |       |           |       |
|------------------|--------------|-----------|-------|-----------|-------|
| <b>2,150,441</b> | <b>100.0</b> | 1,738,138 | 100.0 | 1,860,758 | 100.0 |
|------------------|--------------|-----------|-------|-----------|-------|

*For footnotes, see page 22.*

[Back to Contents](#)**Personal Financial Services**

Profit before tax

|  | Half-year to  |               |               |
|--|---------------|---------------|---------------|
|  | 30 June       | 30 June       | 31 December   |
|  | 2007          | 2006          | 2006          |
|  | US\$m         | US\$m         | US\$m         |
| Net interest income  | 13,998        | 12,736        | 13,340        |
| Net fee income   | 5,523         | 4,285         | 4,477         |
| Trading income excluding net interest income                   | 1             | 314           | 77            |
| Net interest income on trading activities                      | 92            | 103           | 117           |
| Net trading income <sup>2</sup>                                | 93            | 417           | 194           |
| Net income from financial instruments designated at fair value | 796           | 120           | 619           |
| Gains less losses from financial investments                   | 60            | 66            | 12            |
| Dividend income  | 41            | 8             | 23            |
| Net earned insurance premiums                                  | 3,735         | 2,517         | 2,613         |
| Other operating income   | 255           | 343           | 439           |
| <b>Total operating income</b>                                  | <b>24,501</b> | <b>20,492</b> | <b>21,717</b> |
| Net insurance claims <sup>3</sup>                              | (3,605)       | (1,975)       | (2,390)       |
| <b>Net operating income<sup>4</sup></b>                        | <b>20,896</b> | <b>18,517</b> | <b>19,327</b> |
| Loan impairment charges and other credit risk provisions       | (5,928)       | (3,709)       | (6,240)       |
| <b>Net operating income</b>                                    | <b>14,968</b> | <b>14,808</b> | <b>13,087</b> |
| Total operating expenses                                       | (10,452)      | (9,073)       | (9,745)       |
| <b>Operating profit</b>  | <b>4,516</b>  | <b>5,735</b>  | <b>3,342</b>  |
| Share of profit in associates and joint ventures               | 213           | 173           | 207           |
| <b>Profit before tax</b>                                       | <b>4,729</b>  | <b>5,908</b>  | <b>3,549</b>  |
| <b>By geographical region</b>                                  |               |               |               |
| Europe   | 604           | 912           | 997           |
| Hong Kong  | 1,898         | 1,420         | 1,460         |
| Rest of Asia-Pacific   | 351           | 205           | 272           |
| North America <sup>5</sup>                                     | 1,488         | 3,017         | 374           |
| Latin America <sup>5</sup>                                     | 388           | 354           | 446           |
| Profit before tax  | 4,729         | 5,908         | 3,549         |
|  | %             | %             | %             |
| Share of HSBC's profit before tax                              | 33.4          | 47.2          | 37.1          |

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|                       |             |      |      |
|-----------------------|-------------|------|------|
| Cost efficiency ratio | <b>50.0</b> | 49.0 | 50.4 |
|-----------------------|-------------|------|------|

### Balance sheet data<sup>1</sup>

|                                       | US\$m          | US\$m   | US\$m   |
|---------------------------------------|----------------|---------|---------|
| Loans and advances to customers (net) | <b>460,196</b> | 424,796 | 448,545 |
| Total assets                          | <b>577,402</b> | 511,552 | 546,568 |
| Customer accounts                     | <b>416,525</b> | 355,627 | 388,468 |

*For footnotes, see page 22.*

### Business highlights

- Pre-tax profits from Personal Financial Services were US\$4,729 million, a decrease of 20 per cent compared with the first half of 2006. This was primarily caused by higher loan impairment charges in the US. Outside the US, pre-tax profits grew strongly in Hong Kong, Brazil, the United Arab Emirates and across the rest of Asia-Pacific. On an underlying basis, profit before tax was 22 per cent lower.
- HSBC Premier, the Group's personal banking service targeted at mass-affluent customers was relaunched simultaneously in 35 markets in May 2007. With a new logo and bespoke look and feel, HSBC Premier offers a comprehensive and consistent proposition to affluent customers across many markets, supported by 250 International Premier Centres worldwide. By the end of June 2007, some 75,000 new customers had signed up to the service.
- HSBC Direct, the Group's online banking and savings proposition, was launched in South Korea and Canada during the first half of 2007, following Taiwan in September 2006 and the US a year earlier.
- In Asia, over 120,000 customers are now using HSBC Direct with savings balances exceeding US\$900 million. The HSBC Direct business in the US attracted 225,000 new customers and US\$4.8 billion of balances in the first half of 2007. HSBC intends to introduce HSBC Direct in other markets in 2008.
- The Group's new strategic Internet Banking platform, developed to meet customer needs across all Personal Financial Services markets, was rolled out in Hong Kong, bringing the number of markets in which it is deployed to 21. The platform will continue to be rolled out to new markets over the next 18 months.
- In the UK, 12 per cent of personal loan applications are now being completed online using a new automated personal loan system which enables approved loans to be paid into customers' accounts within minutes of their application.
- In Hong Kong, over four million stock trades were completed in the first half of 2007, 83 per cent of which were online. Online trades were up 98 per cent on the second half of 2006.

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HSBC HOLDINGS PLC

**Business Review** (continued)**Commercial Banking**

Profit before tax

|  | Half-year to             |                          |                              |
|--|--------------------------|--------------------------|------------------------------|
|  | 30 June<br>2007<br>US\$m | 30 June<br>2006<br>US\$m | 31 December<br>2006<br>US\$m |
| Net interest income  | 4,286                    | 3,515                    | 3,999                        |
| Net fee income   | 1,904                    | 1,555                    | 1,652                        |
| Trading income excluding net interest income                             | 121                      | 91                       | 113                          |
| Net interest income on trading activities                                | 13                       | 5                        | 15                           |
| Net trading income <sup>2</sup>  | 134                      | 96                       | 128                          |
| Net income/(expense) from financial instruments designated at fair value | (24)                     | (40)                     | 18                           |
| Gains less losses from financial investments                             | 25                       | 23                       | 21                           |
| Dividend income  | 4                        | 2                        | 4                            |
| Net earned insurance premiums  | 205                      | 128                      | 130                          |
| Other operating income   | 2                        | 126                      | 124                          |
| <b>Total operating income</b>  | <b>6,536</b>             | <b>5,405</b>             | <b>6,076</b>                 |
| Net insurance claims <sup>3</sup>  | 44                       | (42)                     | (54)                         |
| <b>Net operating income<sup>4</sup></b>                                  | <b>6,580</b>             | <b>5,363</b>             | <b>6,022</b>                 |
| Loan impairment charges and other credit risk provisions                 | (431)                    | (260)                    | (437)                        |
| <b>Net operating income</b>  | <b>6,149</b>             | <b>5,103</b>             | <b>5,585</b>                 |
| Total operating expenses   | (2,907)                  | (2,385)                  | (2,594)                      |
| <b>Operating profit</b>  | <b>3,242</b>             | <b>2,718</b>             | <b>2,991</b>                 |
| Share of profit in associates and joint ventures                         | 180                      | 144                      | 144                          |
| <b>Profit before tax</b>   | <b>3,422</b>             | <b>2,862</b>             | <b>3,135</b>                 |
| <b>By geographical region</b>  |                          |                          |                              |
| Europe   | 1,236                    | 1,076                    | 1,158                        |
| Hong Kong  | 760                      | 587                      | 734                          |
| Rest of Asia-Pacific   | 597                      | 498                      | 536                          |
| North America <sup>5</sup>   | 477                      | 464                      | 493                          |
| Latin America <sup>5</sup>   | 352                      | 237                      | 214                          |

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|                                       |                |         |         |
|---------------------------------------|----------------|---------|---------|
| Profit before tax                     | <b>3,422</b>   | 2,862   | 3,135   |
|                                       | %              | %       | %       |
| Share of HSBC's profit before tax     | <b>24.2</b>    | 22.9    | 32.8    |
| Cost efficiency ratio                 | <b>44.2</b>    | 44.5    | 43.1    |
| <b>Balance sheet data<sup>1</sup></b> |                |         |         |
|                                       | <b>US\$m</b>   | US\$m   | US\$m   |
| Loans and advances to customers (net) | <b>185,923</b> | 152,318 | 172,976 |
| Total assets                          | <b>225,763</b> | 186,195 | 213,450 |
| Customer accounts                     | <b>205,002</b> | 165,706 | 190,853 |

*For footnotes, see page 22.*

### Business highlights

- Pre-tax profit increased by 20 per cent to US\$3,422 million, representing 24 per cent of Group profits. Revenue growth of 23 per cent resulted from improved income from loans and advances, fees and customer deposits. Cost growth reflected business expansion in India, mainland China and the Middle East. These figures also reflected the inclusion for the first time of Grupo Banistmo S.A.'s ( Grupo Banistmo ) operations in Latin America. The cost efficiency ratio improved from 44.5 per cent to 44.2 per cent. On an underlying basis, pre-tax profits were 14 per cent higher than in the first half of 2006.
- Total customer numbers rose by 3 per cent to 2.7 million, with the strongest growth in Latin America.
- Small business banking income growth was greatest in emerging markets, with Turkey benefiting from dedicated centres opened in 2006 and Mexico from product development. In addition, strong growth in Hong Kong resulted from promotions and a buoyant market. The Hong Kong Chamber for Small and Medium Business again recognised HSBC with its Best Partner Award. In the US, HSBC's Green Campaign targeted new customers with a package of incentives for customers switching to online bill payments.
- HSBC continued to develop direct channels. The number of customers actively using HSBC's internet banking services increased by 11 per cent. In Asia, internet banking migrated to a new platform with enhanced sales capabilities. In the UK, the Business Direct proposition, launched in September 2006, attracted 22,000 new customers in the first half of 2007. Globally, the number of Commercial Banking customers using HSBCnet also grew rapidly.
- In international business, HSBC added seven new International Banking Centres dedicated to cross-border account opening, a network that now covers 23 countries. The Global Links cross-border referral system generated 37 per cent more referrals. To support customers with cross-border operations, credit processes were further streamlined. HSBC's trade credentials were reinforced, winning Best Online Trade Finance Provider for the first time, and Best Factor for the fifth successive year, in *Euromoney* Trade Finance Awards for Excellence.

[Back to Contents](#)**Corporate, Investment Banking and Markets**

Profit before tax

|  | Half-year to |              |              |
|--|--------------|--------------|--------------|
|  | 30 June      | 30 June      | 31 December  |
|  | 2007         | 2006         | 2006         |
|  | US\$m        | US\$m        | US\$m        |
| Net interest income  | 1,847        | 1,394        | 1,774        |
| Net fee income   | 2,264        | 1,810        | 1,908        |
| Trading income excluding net interest income                             | 3,048        | 2,613        | 2,277        |
| Net interest expense on trading activities                               | (151)        | (117)        | (262)        |
| Net trading income <sup>2</sup>  | 2,897        | 2,496        | 2,015        |
| Net income/(expense) from financial instruments designated at fair value | 11           | 47           | (27)         |
| Gains less losses from financial investments                             | 768          | 269          | 265          |
| Dividend income  | 175          | 147          | 88           |
| Net earned insurance premiums  | 46           | 41           | 32           |
| Other operating income   | 529          | 578          | 800          |
| <b>Total operating income</b>  | <b>8,537</b> | <b>6,782</b> | <b>6,855</b> |
| Net insurance claims <sup>3</sup>  | (38)         | (31)         | (31)         |
| <b>Net operating income<sup>4</sup></b>                                  | <b>8,499</b> | <b>6,751</b> | <b>6,824</b> |
| Net loan impairment recoveries and other credit risk provisions          | 24           | 109          | 10           |
| <b>Net operating income</b>  | <b>8,523</b> | <b>6,860</b> | <b>6,834</b> |
| Total operating expenses   | (4,479)      | (3,740)      | (4,251)      |
| <b>Operating profit</b>  | <b>4,044</b> | <b>3,120</b> | <b>2,583</b> |
| Share of profit in associates and joint ventures                         | 114          | 24           | 79           |
| <b>Profit before tax</b>   | <b>4,158</b> | <b>3,144</b> | <b>2,662</b> |
| <b>By geographical region</b>  |              |              |              |
| Europe   | 1,674        | 1,202        | 1,102        |
| Hong Kong  | 697          | 477          | 478          |
| Rest of Asia-Pacific   | 1,098        | 839          | 810          |
| North America <sup>5</sup>   | 436          | 349          | 74           |
| Latin America <sup>5</sup>   | 253          | 277          | 198          |
| Profit before tax  | 4,158        | 3,144        | 2,662        |
|  | %            | %            | %            |



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|                                   |      |      |      |
|-----------------------------------|------|------|------|
| Share of HSBC's profit before tax | 29.4 | 25.1 | 27.8 |
| Cost efficiency ratio             | 52.7 | 55.4 | 62.3 |

*For footnotes, see page 22.*

### Business highlights

- Pre-tax profit increased by 32 per cent to US\$4,158 million, driven by a 26 per cent rise in total operating income. Strong performance across major product lines was due to past investment in building the systems and sales infrastructure to support the continued successful delivery of HSBC's emerging markets-led and financing-focused wholesale banking strategy. Asia and Latin America accounted for 49 per cent of profit before tax. The cost efficiency ratio improved by 2.7 percentage points, reflecting a significant acceleration of revenue growth ahead of cost growth. The increase in operating expenses was partly driven by performance-related compensation, which rose in line with the robust revenue growth. Higher operational costs also reflected volume increases, particularly in securities services and payments and cash management. On an underlying basis, pre-tax profits were 27 per cent higher than in the first half of 2006.
- HSBC's extensive geographical network and its recently enhanced product capabilities enabled the tailored delivery of risk management, investment, financing and other solutions to clients around the world. HSBC was named global Best Risk Management House and Best Cash Management House in the *Euromoney* 2007 Awards for Excellence. In regional *Euromoney* awards, HSBC was also named Best Risk Management House in the Middle East, Best FX House in Asia and, for the 10th consecutive year, Best Risk Management House in Asia.
- In Global Markets, total operating income increased by 26 per cent. The structured derivatives business gained momentum as investment in technical expertise and systems enabled HSBC to address a broader spectrum of client needs.

Foreign exchange reported gains from growth in the core business and increased customer activity, against the backdrop of a weakening US dollar. Strong gains were reported across emerging markets as HSBC continued to harness the Group's global distribution network.

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HSBC HOLDINGS PLC

**Business Review** (continued)

Management view of total operating income

|                                    | Half-year to |         |             |
|------------------------------------|--------------|---------|-------------|
|                                    | 30 June      | 30 June | 31 December |
|                                    | 2007         | 2006    | 2006        |
|                                    | US\$m        | US\$m   | US\$m       |
| <b>Global Markets</b>              | <b>3,590</b> | 2,849   | 2,684       |
| Foreign exchange                   | 909          | 848     | 704         |
| Credit and rates                   | 653          | 694     | 640         |
| Structured derivatives             | 765          | 455     | 419         |
| Equities <sup>2</sup>              | 408          | 196     | 201         |
| HSBC Securities Services           | 855          | 656     | 720         |
| <b>Global Banking</b>              | <b>2,209</b> | 1,996   | 2,100       |
| Investment banking                 | 592          | 491     | 674         |
| Lending                            | 685          | 713     | 560         |
| Payments and cash management       | 751          | 609     | 648         |
| Other transaction services         | 181          | 183     | 218         |
| <b>Balance Sheet Management</b>    | <b>521</b>   | 366     | 347         |
| <b>Group Investment Businesses</b> | <b>636</b>   | 595     | 471         |
| <b>Principal Investments</b>       | <b>755</b>   | 292     | 394         |
| <b>Other<sup>3</sup></b>           | <b>826</b>   | 684     | 859         |
| <b>Total operating income</b>      | <b>8,537</b> | 6,782   | 6,855       |

Balance sheet data<sup>4</sup>

Loans and advances to:

|   |                  |         |         |
|---|------------------|---------|---------|
| customers (net)   | 241,602          | 203,159 | 210,220 |
| banks (net)   | 183,708          | 136,912 | 156,548 |
| <b>Total assets</b>   | <b>1,220,316</b> | 940,177 | 994,436 |
| Customer accounts   | 265,739          | 235,329 | 235,965 |
| Trading assets, financial instruments designated at fair value, and financial investments | 601,883          | 448,595 | 487,943 |
| Deposits by banks   | 121,744          | 77,584  | 92,954  |

1 The comparatives have been restated to reflect the current management view. The results of HSBC Trinkaus & Burkhardt AG, previously reported in Other, are now included in the appropriate business lines above. Principal Investments includes private equity, and HSBC Specialist Investment Ltd previously reported in Group Investment Businesses.

2 Equities includes a total gain of US\$107 million from the disposal of HSBC's investments in Euronext N.V. and the Montreal Exchange.

3 Other includes net interest earned on free capital held in CIBM not assigned to products.

4 Third party only.

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Equities recorded a significant increase on the comparable period in 2006, partly driven by the strength of major stock indices. Revenue from the credit and rates business declined due to widening credit spreads. Securities services benefited from increased customer volumes in higher-value products and strong income growth in emerging markets. Assets under custody rose by 32 per cent.

- In Global Banking, total operating income rose by US\$213 million. Income from financing transactions rose partly due to higher fee income in leveraged and acquisition finance, principally in the UK. Payments and cash management delivered a strong performance across most regions, driven by growth in client deposits.

HSBC's strong focus on emerging markets and financing was highlighted by several notable transactions, including cross-border investment banking mandates for Singapore Telecommunications US\$758 million acquisition of a 30 per cent stake in Warid Telecom of Pakistan; National Titanium Dioxide of Saudi Arabia's S\$1.2 billion acquisition of Lyondell Chemical's inorganic chemical business in the US; and Dubai Drydocks S\$650 million acquisition of Pan-United Marine of Singapore.

HSBC acted as lead arranger of US\$9.2 billion of facilities for the acquisition of GE Plastics by Saudi Basic Industries; 2.25 billion of facilities backing the acquisition of Mölnlycke Health Care of Sweden by Investor AB; and facilities for Macquarie of £1.8 billion for the acquisition of O2 Airwave and £3.4 billion for the acquisition of National Grid Wireless.

In debt capital markets, HSBC ranked first in the Asian local currency bond league table compiled by Bloomberg, first in the sterling bond league table and sixth in the international bond league table. HSBC ranked sixth in the Asia (ex Japan) league table for equity initial public offerings (IPOs).

- In Balance Sheet Management, total operating income increased by 42 per cent. This was driven by a recovery in revenues in Asia.
- Gains from realisations increased in Principal Investments as a result of an increase in the number of disposals and higher exit multiples. The structure of Principal Investments was realigned to position the business for further development.
- Group Investment Businesses' operating income rose by 7 per cent due to continued strong contribution from performance fees coupled with a modest growth in funds under management, mainly relating to emerging market funds. Noteworthy successes included the development of Latin American equity fund sales in Europe and Asia-Pacific, multi-manager business globally and landmark pension fund mandates won in Europe and North America.

[Back to Contents](#)**Private Banking**

Profit before tax

|  | Half-year to |              |              |
|--|--------------|--------------|--------------|
|  | 30 June      | 30 June      | 31 December  |
|  | 2007         | 2006         | 2006         |
|  | US\$m        | US\$m        | US\$m        |
| Net interest income  | 567          | 482          | 529          |
| Net fee income   | 811          | 705          | 618          |
| Trading income excluding net interest income                   | 255          | 209          | 153          |
| Net interest income/ (expense) on trading activities           | 4            | 7            | (5)          |
| Net trading income <sup>2</sup>                                | 259          | 216          | 148          |
| Net income from financial instruments designated at fair value |              |              | 1            |
| Gains less losses from financial investments                   | 45           | 28           | 138          |
| Dividend income  | 5            | 4            | 1            |
| Other operating income   | 31           | 25           | 36           |
| <b>Total operating income</b>                                  | <b>1,718</b> | <b>1,460</b> | <b>1,471</b> |
| Net insurance claims <sup>3</sup>                              |              |              |              |
| <b>Net operating income<sup>4</sup></b>                        | <b>1,718</b> | <b>1,460</b> | <b>1,471</b> |
| Loan impairment charges and other credit risk provisions       | (9)          | (29)         | (4)          |
| <b>Net operating income</b>                                    | <b>1,709</b> | <b>1,431</b> | <b>1,467</b> |
| Total operating expenses                                       | (929)        | (831)        | (854)        |
| <b>Operating profit</b>  | <b>780</b>   | <b>600</b>   | <b>613</b>   |
| Share of profit in associates and joint ventures               |              |              | 1            |
| <b>Profit before tax</b>                                       | <b>780</b>   | <b>600</b>   | <b>614</b>   |
| <b>By geographical region</b>                                  |              |              |              |
| Europe   | 493          | 388          | 417          |
| Hong Kong  | 161          | 123          | 78           |
| Rest of Asia-Pacific   | 56           | 48           | 32           |
| North America <sup>5</sup>                                     | 60           | 38           | 76           |
| Latin America <sup>5</sup>                                     | 10           | 3            | 11           |
| <b>Profit before tax</b>                                       | <b>780</b>   | <b>600</b>   | <b>614</b>   |
|  | %            | %            | %            |
| Share of HSBC's profit before tax                              | 5.5          | 4.8          | 6.4          |
| Cost efficiency ratio  | 54.1         | 56.9         | 58.1         |

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### Balance sheet data<sup>1</sup>

|                                       | US\$m         | US\$m  | US\$m  |
|---------------------------------------|---------------|--------|--------|
| Loans and advances to customers (net) | <b>37,863</b> | 31,903 | 34,297 |
| Total assets                          | <b>81,916</b> | 67,643 | 73,026 |
| Customer accounts                     | <b>91,228</b> | 76,496 | 80,303 |

For footnotes, see page 22.

### Business highlights

- Pre-tax profits grew by 30 per cent to US\$780 million, as HSBC's competitive offerings proved attractive to clients in an economic environment that continued to be conducive to wealth management services. On an underlying basis, profit before tax was 27 per cent higher than in the first half of 2006.
- Private Banking demonstrated success in implementing HSBC's strategy of joining up the Group and harnessing the strengths of its main businesses. Cross-referrals with other customer groups were positive, with almost US\$2 billion in total client assets referred into Private Banking, and anticipated fees for the Group from mandated deals referred by Private Banking to CIBM in the first six months of 2007 reaching US\$75 million.
- Client assets, which provide an indicator of overall Private Banking volumes and include funds under management, cash deposits and certain on-balance sheet trust assets, rose by 11 per cent, or 10 per cent on an underlying basis, compared with 31 December 2006, to reach US\$370 billion.

#### Half-year to

|                        | <b>30 June<br/>2007<br/>US\$bn</b> | 30 June<br>2006<br>US\$bn | 31 December<br>2006<br>US\$bn |
|------------------------|------------------------------------|---------------------------|-------------------------------|
| At beginning of period | <b>333</b>                         | 273                       | 305                           |
| Net new money          | <b>17</b>                          | 19                        | 15                            |
| Value change           | <b>12</b>                          | 5                         | 16                            |
| Exchange/other         | <b>8</b>                           | 8                         | (3)                           |
| At end of period       | <b>370</b>                         | 305                       | 333                           |

- Many of HSBC's competitors publish a measure of assets managed which also includes non-financial assets held off-balance sheet in client trusts. HSBC refers to this measure as total client assets and, at 30 June 2007, this amounted to US\$442 billion, an 8 per cent increase since 31 December 2006.
- Amanah Investment Solutions, a *shariah* (Islamic law)-compliant multi-manager fund product, was added to the successful Investment Solutions offerings.
- Private Banking clients took up approximately one-third of the US\$1.1 billion launch of HSBC's MultiAlpha China Fund.
- The HSBC Special Opportunities Fund, a fund of hedge funds that invests in long-term alternative strategies, raised over US\$465 million.

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HSBC HOLDINGS PLC

**Business Review** (continued)**Other**

Profit/(loss) before tax

|  | Half-year to |              |              |
|--|--------------|--------------|--------------|
|  | 30 June      | 30 June      | 31 December  |
|  | 2007         | 2006         | 2006         |
|  | US\$m        | US\$m        | US\$m        |
| Net interest expense   | (291)        | (292)        | (333)        |
| Net fee income/(expense)   | (7)          | 25           | 147          |
| Trading expense excluding net interest income                            | (74)         | (115)        | (113)        |
| Net interest income on trading activities                                | 25           | 47           | 35           |
| Net trading expense <sup>2</sup>   | (49)         | (68)         | (78)         |
| Net income/(expense) from financial instruments designated at fair value | 91           | 133          | (214)        |
| Gains less losses from financial investments                             | 101          | 107          | 40           |
| Gains arising from dilution of interests in associates                   | 1,076        |              |              |
| Dividend income  | 27           | 61           | 2            |
| Net earned insurance premiums  | (9)          | 148          | 59           |
| Other operating income   | 1,667        | 1,544        | 1,710        |
| <b>Total operating income</b>  | <b>2,606</b> | <b>1,658</b> | <b>1,333</b> |
| Net insurance claims <sup>3</sup>  |              | (101)        | (80)         |
| <b>Net operating income<sup>4</sup></b>                                  | <b>2,606</b> | <b>1,557</b> | <b>1,253</b> |
| Loan impairment charges and other credit risk provisions                 | (2)          | (1)          | (12)         |
| <b>Net operating income</b>  | <b>2,604</b> | <b>1,556</b> | <b>1,241</b> |
| Total operating expenses   | (1,650)      | (1,573)      | (1,686)      |
| <b>Operating profit/(loss)</b>   | <b>954</b>   | <b>(17)</b>  | <b>(445)</b> |
| Share of profit in associates and joint ventures                         | 116          | 20           | 54           |
| <b>Profit/(loss) before tax</b>  | <b>1,070</b> | <b>3</b>     | <b>(391)</b> |
| <b>By geographical region</b>  |              |              |              |
| Europe   | 43           | 22           | (300)        |
| Hong Kong  | (186)        | 47           | (222)        |
| Rest of Asia-Pacific   | 1,242        | 67           | 220          |
| North America <sup>5</sup>   | (26)         | (127)        | (90)         |

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|                                       |               |        |        |
|---------------------------------------|---------------|--------|--------|
| Latin America <sup>5</sup>            | (3)           | (6)    | 1      |
| Profit/(loss) before tax              | <b>1,070</b>  | 3      | (391)  |
|                                       | %             | %      | %      |
| Share of HSBC's profit before tax     | <b>7.5</b>    |        | (4.1)  |
| Cost efficiency ratio                 | <b>63.3</b>   | 101.0  | 134.6  |
| Balance sheet data <sup>1</sup>       |               |        |        |
|                                       | US\$m         | US\$m  | US\$m  |
| Loans and advances to customers (net) | <b>2,517</b>  | 2,033  | 2,095  |
| Total assets                          | <b>45,044</b> | 32,571 | 33,278 |
| Customer accounts                     | <b>2,338</b>  | 584    | 1,245  |

For footnotes, see page 22.

Notes

- For a description of the main items reported under 'Other', see footnote 6 on page 22.
- HSBC recorded dilution gains of US\$1,076 million following share offerings made in Shanghai by HSBC's three associates: Ping An Insurance (Group) Company of China, Limited ('Ping An Insurance'), Bank of Communications Limited ('Bank of Communications') and Industrial Bank Co. Limited ('Industrial Bank'), which all successfully raised new capital. The consequent dilution of HSBC's interests was considerably less than its share of the new monies raised, resulting in the gains recognised. For further details see Note 19 on the Financial Statements.
- The results of the HSBC Insurance Brokers group were allocated to HSBC's customer groups in the first half of 2007, having been reported within Other in 2006. As a consequence, net operating income before loan impairment charges and operating expenses were US\$205 million and US\$178 million, respectively, lower than in the first half of 2006, resulting in a US\$27 million reduction in profit before tax.
- This segment includes fair value movements of US\$284 million on HSBC's own debt in issue and related swaps. This movement is largely a consequence of higher medium to longer-term interest rates in the UK and a widening of credit spreads in North America.
- The Group Service Centres continued to grow in the first half of 2007, their nearly 29,000 employees providing services to 40 different HSBC companies, handling on average 462,000 calls and processing 1.7 million transactions every day. The Group Service Centres provide a range of services from general processing work, telephone banking services and value-added services for analytical and financial modelling for certain lines of business. Costs rose by 32 per cent, substantially all of which were recharged to HSBC's customer groups and global businesses. During the first half of 2007, three additional Group Service Centres became operational, with a further two under development.

[Back to Contents](#)**Analysis by customer group and global business**

Profit/(loss) before tax and balance sheet data

Half-year to 30 June 2007

| Total  | Personal      | Commercial   | Corporate,   | Private      | Other <sup>6</sup> | Inter-         | Total         |
|--|---------------|--------------|--------------|--------------|--------------------|----------------|---------------|
|  | Financial     | Banking      | Investment   | Banking      |                    | segment        |               |
|  | Services      |              | Banking &    |              |                    | elimination    |               |
|  | US\$m         | US\$m        | Markets      | US\$m        | US\$m              | US\$m          | US\$m         |
| Net interest income/(expense)  | 13,998        | 4,286        | 1,847        | 567          | (291)              | (2,177)        | 18,230        |
| Net fee income/(expense)   | 5,523         | 1,904        | 2,264        | 811          | (7)                |                | 10,495        |
| Trading income/(expense) excluding net interest income                   | 1             | 121          | 3,048        | 255          | (74)               |                | 3,351         |
| Net interest income/(expense) on trading activities                      | 92            | 13           | (151)        | 4            | 25                 | 2,177          | 2,160         |
| Net trading income/(expense) <sup>2</sup>                                | 93            | 134          | 2,897        | 259          | (49)               | 2,177          | 5,511         |
| Net income/(expense) from financial instruments designated at fair value | 796           | (24)         | 11           |              | 91                 |                | 874           |
| Gains less losses from financial investments                             | 60            | 25           | 768          | 45           | 101                |                | 999           |
| Gains arising from dilution of interests in associates                   |               |              |              |              | 1,076              |                | 1,076         |
| Dividend income  | 41            | 4            | 175          | 5            | 27                 |                | 252           |
| Net earned insurance premiums  | 3,735         | 205          | 46           |              | (9)                |                | 3,977         |
| Other operating income   | 255           | 2            | 529          | 31           | 1,667              | (1,806)        | 678           |
| <b>Total operating income</b>  | <b>24,501</b> | <b>6,536</b> | <b>8,537</b> | <b>1,718</b> | <b>2,606</b>       | <b>(1,806)</b> | <b>42,092</b> |
| Net insurance claims <sup>3</sup>  | (3,605)       | 44           | (38)         |              |                    |                | (3,599)       |
| <b>Net operating income<sup>4</sup></b>                                  | <b>20,896</b> | <b>6,580</b> | <b>8,499</b> | <b>1,718</b> | <b>2,606</b>       | <b>(1,806)</b> | <b>38,493</b> |
| Loan impairment (charges)/recoveries and other credit risk provisions    | (5,928)       | (431)        | 24           | (9)          | (2)                |                | (6,346)       |
| <b>Net operating income</b>  | <b>14,968</b> | <b>6,149</b> | <b>8,523</b> | <b>1,709</b> | <b>2,604</b>       | <b>(1,806)</b> | <b>32,147</b> |
| Total operating expenses   | (10,452)      | (2,907)      | (4,479)      | (929)        | (1,650)            | 1,806          | (18,611)      |
| <b>Operating profit</b>  | <b>4,516</b>  | <b>3,242</b> | <b>4,044</b> | <b>780</b>   | <b>954</b>         |                | <b>13,536</b> |
| Share of profit in associates and joint ventures                         | 213           | 180          | 114          |              | 116                |                | 623           |
| <b>Profit before tax</b>   | <b>4,729</b>  | <b>3,422</b> | <b>4,158</b> | <b>780</b>   | <b>1,070</b>       |                | <b>14,159</b> |
|  | %             | %            | %            | %            | %                  |                | %             |
| Share of HSBC's profit before tax  | 33.4          | 24.2         | 29.4         | 5.5          | 7.5                |                | 100.0         |
| Cost efficiency ratio  | 50.0          | 44.2         | 52.7         | 54.1         | 63.3               |                | 48.3          |



**Balance sheet data**

|   | US\$m   | US\$m   | US\$m     | US\$m  | US\$m  | US\$m     |
|---|---------|---------|-----------|--------|--------|-----------|
| Loans and advances to customers (net)   | 460,196 | 185,923 | 241,602   | 37,863 | 2,517  | 928,101   |
| Total assets  | 577,402 | 225,763 | 1,220,316 | 81,916 | 45,044 | 2,150,441 |
| Customer accounts   | 416,525 | 205,002 | 265,739   | 91,228 | 2,338  | 980,832   |
| Loans and advances to banks (net) <sup>7</sup>  |         |         | 183,708   |        |        |           |
| Trading assets, financial assets designated at fair value, and financial investments <sup>7</sup> |         |         | 601,883   |        |        |           |
| Deposits by banks <sup>7</sup>  |         |         | 121,744   |        |        |           |

*For footnotes, see page 22.*

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HSBC HOLDINGS PLC

**Business Review** (continued)

Profit/(loss) before tax and balance sheet data (continued)

Half-year to 30 June 2006

| <b>Total</b>   | Personal<br>Financial<br>Services<br>US\$m | Commercial<br>Banking<br>US\$m | Corporate,<br>Investment<br>Banking &<br>Markets<br>US\$m | Private<br>Banking<br>US\$m | Other <sup>6</sup><br>US\$m | Inter-<br>segment<br>elimination<br>US\$m | Total<br>US\$m  |
|--|--|--------------------------------|---|-----------------------------|-----------------------------|---|-----------------|
| Net interest income/(expense)  | 12,736                                     | 3,515                          | 1,394   | 482                         | (292)                       | (1,104)                                   | 16,731          |
| Net fee income   | 4,285                                      | 1,555                          | 1,810   | 705                         | 25                          |   | 8,380           |
| Trading income/(expense) excluding net interest income                   | 314  | 91                             | 2,613   | 209                         | (115)                       |   | 3,112           |
| Net interest income/(expense) on trading activities                      | 103  | 5                              | (117)   | 7                           | 47                          | 1,104                                     | 1,149           |
| Net trading income/(expense) <sup>2</sup>                                | 417  | 96                             | 2,496   | 216                         | (68)                        | 1,104                                     | 4,261           |
| Net income/(expense) from financial instruments designated at fair value | 120  | (40)                           | 47  |                             | 133                         |   | 260             |
| Gains less losses from financial investments                             | 66   | 23                             | 269   | 28                          | 107                         |   | 493             |
| Dividend income  | 8  | 2                              | 147   | 4                           | 61                          |   | 222             |
| Net earned insurance premiums  | 2,517                                      | 128                            | 41  |                             | 148                         |   | 2,834           |
| Other operating income   | 343  | 126                            | 578   | 25                          | 1,544                       | (1,463)                                   | 1,153           |
| <b>Total operating income</b>  | <b>20,492</b>                              | <b>5,405</b>                   | <b>6,782</b>  | <b>1,460</b>                | <b>1,658</b>                | <b>(1,463)</b>                            | <b>34,334</b>   |
| Net insurance claims <sup>3</sup>  | (1,975)                                    | (42)                           | (31)  |                             | (101)                       |   | (2,149)         |
| <b>Net operating income<sup>4</sup></b>                                  | <b>18,517</b>                              | <b>5,363</b>                   | <b>6,751</b>  | <b>1,460</b>                | <b>1,557</b>                | <b>(1,463)</b>                            | <b>32,185</b>   |
| Loan impairment (charges)/recoveries and other credit risk provisions    | (3,709)                                    | (260)                          | 109   | (29)                        | (1)                         |   | (3,890)         |
| <b>Net operating income</b>  | <b>14,808</b>                              | <b>5,103</b>                   | <b>6,860</b>  | <b>1,431</b>                | <b>1,556</b>                | <b>(1,463)</b>                            | <b>28,295</b>   |
| <b>Total operating expenses</b>  | <b>(9,073)</b>                             | <b>(2,385)</b>                 | <b>(3,740)</b>  | <b>(831)</b>                | <b>(1,573)</b>              | <b>1,463</b>                              | <b>(16,139)</b> |
| <b>Operating profit/(loss)</b>   | <b>5,735</b>                               | <b>2,718</b>                   | <b>3,120</b>  | <b>600</b>                  | <b>(17)</b>                 |   | <b>12,156</b>   |
| Share of profit in associates and joint ventures                         | 173  | 144                            | 24  |                             | 20                          |   | 361             |
| <b>Profit before tax</b>   | <b>5,908</b>                               | <b>2,862</b>                   | <b>3,144</b>  | <b>600</b>                  | <b>3</b>                    |   | <b>12,517</b>   |
|  | %  | %                              | %   | %                           | %                           |   | %               |
| Share of HSBC's profit before tax  | 47.2                                       | 22.9                           | 25.1  | 4.8                         |                             |   | 100.0           |
| Cost efficiency ratio  | 49.0                                       | 44.5                           | 55.4  | 56.9                        | 101.0                       |   | 50.1            |

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Balance sheet data<sup>1</sup>

|   | US\$m   | US\$m   | US\$m   | US\$m  | US\$m  | US\$m     |
|---|---------|---------|---------|--------|--------|-----------|
| Loans and advances to customers (net)   | 424,796 | 152,318 | 203,159 | 31,903 | 2,033  | 814,209   |
| Total assets  | 511,552 | 186,195 | 940,177 | 67,643 | 32,571 | 1,738,138 |
| Customer accounts   | 355,627 | 165,706 | 235,329 | 76,496 | 584    | 833,742   |
| Loans and advances to banks (net) <sup>7</sup>  |         |         | 136,912 |        |        |           |
| Trading assets, financial assets designated at fair value, and financial investments <sup>7</sup> |         |         | 448,595 |        |        |           |
| Deposits by banks <sup>7</sup>  |         |         | 77,584  |        |        |           |

*For footnotes, see page 22.*

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Half-year to 31 December 2006

|   | Personal<br>Financial<br>Services<br>US\$m | Commercial<br>Banking<br>US\$m | Corporate,<br>Investment<br>Banking &<br>Markets<br>US\$m | Private<br>Banking<br>US\$m | Other <sup>6</sup><br>US\$m | Inter-<br>segment<br>elimination<br>US\$m | Total<br>US\$m  |
|---|--|--------------------------------|---|-----------------------------|-----------------------------|---|-----------------|
| <b>Total</b>  |  |                                |   |                             |                             |   |                 |
| Net interest income/ (expense)  | 13,340                                     | 3,999                          | 1,774   | 529                         | (333)                       | (1,554)                                   | 17,755          |
| Net fee income  | 4,477                                      | 1,652                          | 1,908   | 618                         | 147                         |   | 8,802           |
| Trading income/(expense) excluding<br>net interest income                   | 77   | 113                            | 2,277   | 153                         | (113)                       |   | 2,507           |
| Net interest income/(expense) on<br>trading activities                      | 117  | 15                             | (262)   | (5)                         | 35                          | 1,554                                     | 1,454           |
| Net trading income/(expense) <sup>2</sup>                                   | 194  | 128                            | 2,015   | 148                         | (78)                        | 1,554                                     | 3,961           |
| Net income/(expense) from financial<br>instruments designated at fair value | 619  | 18                             | (27)  | 1                           | (214)                       |   | 397             |
| Gains less losses from financial<br>investments                             | 12   | 21                             | 265   | 138                         | 40                          |   | 476             |
| Dividend income   | 23   | 4                              | 88  | 1                           | 2                           |   | 118             |
| Net earned insurance premiums   | 2,613                                      | 130                            | 32  |                             | 59                          |   | 2,834           |
| Other operating income  | 439  | 124                            | 800   | 36                          | 1,710                       | (1,716)                                   | 1,393           |
| <b>Total operating income</b>   | <b>21,717</b>                              | <b>6,076</b>                   | <b>6,855</b>  | <b>1,471</b>                | <b>1,333</b>                | <b>(1,716)</b>                            | <b>35,736</b>   |
| Net insurance claims <sup>3</sup>   | (2,390)                                    | (54)                           | (31)  |                             | (80)                        |   | (2,555)         |
| <b>Net operating income<sup>4</sup></b>                                     | <b>19,327</b>                              | <b>6,022</b>                   | <b>6,824</b>  | <b>1,471</b>                | <b>1,253</b>                | <b>(1,716)</b>                            | <b>33,181</b>   |
| Loan impairment (charges)/ recoveries<br>and other credit risk provisions   | (6,240)                                    | (437)                          | 10  | (4)                         | (12)                        |   | (6,683)         |
| <b>Net operating income</b>   | <b>13,087</b>                              | <b>5,585</b>                   | <b>6,834</b>  | <b>1,467</b>                | <b>1,241</b>                | <b>(1,716)</b>                            | <b>26,498</b>   |
| <b>Total operating expenses</b>   | <b>(9,745)</b>                             | <b>(2,594)</b>                 | <b>(4,251)</b>  | <b>(854)</b>                | <b>(1,686)</b>              | <b>1,716</b>                              | <b>(17,414)</b> |
| <b>Operating profit/(loss)</b>  | <b>3,342</b>                               | <b>2,991</b>                   | <b>2,583</b>  | <b>613</b>                  | <b>(445)</b>                |   | <b>9,084</b>    |
| Share of profit in associates and joint<br>ventures                         | 207  | 144                            | 79  | 1                           | 54                          |   | 485             |
| <b>Profit/(loss) before tax</b>   | <b>3,549</b>                               | <b>3,135</b>                   | <b>2,662</b>  | <b>614</b>                  | <b>(391)</b>                |   | <b>9,569</b>    |
|   | %  | %                              | %   | %                           | %                           |   | %               |
| Share of HSBC's profit before tax   | 37.1                                       | 32.8                           | 27.8  | 6.4                         | (4.1)                       |   | 100.0           |
| Cost efficiency ratio   | 50.4                                       | 43.1                           | 62.3  | 58.1                        | 134.6                       |   | 52.5            |

Balance sheet data<sup>1</sup>

|  | US\$m   | US\$m   | US\$m   | US\$m  | US\$m  | US\$m     |
|--|---------|---------|---------|--------|--------|-----------|
| Loans and advances to customers (net)          | 448,545 | 172,976 | 210,220 | 34,297 | 2,095  | 868,133   |
| Total assets                                   | 546,568 | 213,450 | 994,436 | 73,026 | 33,278 | 1,860,758 |
| Customer accounts                              | 388,468 | 190,853 | 235,965 | 80,303 | 1,245  | 896,834   |
| Loans and advances to banks (net) <sup>7</sup> |         |         | 156,548 |        |        |           |

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|   |         |
|---|---------|
| Trading assets, financial assets<br>designated at fair value, and financial<br>investments <sup>7</sup> | 487,943 |
| Deposits by banks <sup>7</sup>  | 92,954  |

*For footnotes, see page 22.*

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HSBC HOLDINGS PLC

**Business Review** (continued)**Basis of preparation**

Customer group results are presented in accordance with the accounting policies used in the preparation of HSBC's consolidated financial statements. HSBC's operations are closely integrated and, accordingly, the presentation of customer group data includes internal allocations of certain items of income and expense. These allocations include the costs of certain support services and head office functions, to the extent that these can be

meaningfully attributed to operational business lines. While such allocations have been made on a systematic and consistent basis, they necessarily involve a degree of subjectivity.

Where relevant, income and expense amounts presented include the results of inter-segment funding as well as inter-company and inter-business line transactions. All such transactions are undertaken on arm's length terms.

Footnotes to Customer groups and global businesses on pages 12 to 21.

- 1 *Third party only.*
- 2 *In the customer group analyses, net trading income comprises all gains and losses from changes in the fair value of financial assets and financial liabilities classified as held for trading, together with related external and internal interest income and interest expense, and dividends received; in the statutory presentation internal interest income and expense are eliminated.*
- 3 *Net insurance claims incurred and movement in policyholders' liabilities.*
- 4 *Net operating income before loan impairment charges and other credit risk provisions.*
- 5 *In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.*
- 6 *The main items reported under Other are certain property activities, unallocated investment activities including hsbc.com, centrally held investment companies, movements in the fair value of own debt designated at fair value, and HSBC's holding company and financing operations. The results include net interest earned on free capital held centrally and operating costs incurred by the head office operations in providing stewardship and central management services to HSBC. Other also includes the costs incurred by the Group Service Centres and Shared Service Organisations and associated recoveries.*
- 7 *Assets and liabilities which were significant to Corporate, Investment Banking and Markets.*

**Geographical regions**

In the analysis of profit by geographical region that follows, operating income and operating expenses include intra-HSBC items of US\$852 million (first half of 2006: US\$617 million; second half of 2006: US\$877 million).

## Profit before tax

|                      | Half-year to |      |              |      |                  |      |
|----------------------|--------------|------|--------------|------|------------------|------|
|                      | 30 June 2007 |      | 30 June 2006 |      | 31 December 2006 |      |
|                      | US\$m        | %    | US\$m        | %    | US\$m            | %    |
| Europe               | 4,050        | 28.6 | 3,600        | 28.8 | 3,374            | 35.3 |
| Hong Kong            | 3,330        | 23.5 | 2,654        | 21.2 | 2,528            | 26.4 |
| Rest of Asia-Pacific | 3,344        | 23.6 | 1,657        | 13.2 | 1,870            | 19.5 |

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|                            |               |              |        |       |       |       |
|----------------------------|---------------|--------------|--------|-------|-------|-------|
| North America <sup>1</sup> | <b>2,435</b>  | <b>17.2</b>  | 3,741  | 29.9  | 927   | 9.7   |
| Latin America <sup>1</sup> | <b>1,000</b>  | <b>7.1</b>   | 865    | 6.9   | 870   | 9.1   |
|                            | <b>14,159</b> | <b>100.0</b> | 12,517 | 100.0 | 9,569 | 100.0 |

Total assets<sup>2</sup>

|                            | At 30 June 2007  |              | At 30 June 2006 |       | At 31 December 2006 |       |
|----------------------------|------------------|--------------|-----------------|-------|---------------------|-------|
|                            | US\$m            | %            | US\$m           | %     | US\$m               | %     |
| Europe                     | <b>1,040,019</b> | <b>48.3</b>  | 767,608         | 44.2  | 828,701             | 44.6  |
| Hong Kong                  | <b>300,681</b>   | <b>14.0</b>  | 246,781         | 14.2  | 272,428             | 14.6  |
| Rest of Asia-Pacific       | <b>201,123</b>   | <b>9.4</b>   | 168,857         | 9.7   | 167,668             | 9.0   |
| North America <sup>1</sup> | <b>519,693</b>   | <b>24.2</b>  | 495,895         | 28.5  | 511,190             | 27.5  |
| Latin America <sup>1</sup> | <b>88,925</b>    | <b>4.1</b>   | 58,997          | 3.4   | 80,771              | 4.3   |
|                            | <b>2,150,441</b> | <b>100.0</b> | 1,738,138       | 100.0 | 1,860,758           | 100.0 |

1 In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

2 Third party only.

[Back to Contents](#)**Europe**

Profit/(loss) before tax by country within customer groups and global businesses

|                                      | Personal<br>Financial<br>Services<br>US\$m | Commercial<br>Banking<br>US\$m | Corporate,<br>Investment<br>Banking &<br>Markets <sup>1</sup><br>US\$m | Private<br>Banking<br>US\$m | Other<br>US\$m | Total<br>US\$m |
|--------------------------------------|--|--------------------------------|--|-----------------------------|----------------|----------------|
| <b>Half-year to 30 June 2007</b>     |  |                                |  |                             |                |                |
| United Kingdom                       | 384  | 1,001                          | 902  | 198                         | (79)           | 2,406          |
| France <sup>2</sup>                  | 97   | 119                            | 461  | 9                           | 26             | 712            |
| Germany                              |  | 19                             | 125  | 25                          |                | 169            |
| Malta                                | 26   | 35                             | 18   |                             |                | 79             |
| Switzerland                          |  |                                |  | 260                         |                | 260            |
| Turkey                               | 71   | 34                             | 56   |                             |                | 161            |
| Other                                | 26   | 28                             | 112  | 1                           | 96             | 263            |
|                                      | <b>604</b>                                 | <b>1,236</b>                   | <b>1,674</b>   | <b>493</b>                  | <b>43</b>      | <b>4,050</b>   |
| <b>Half-year to 30 June 2006</b>     |  |                                |  |                             |                |                |
| United Kingdom                       | 629  | 851                            | 662  | 106                         | 99             | 2,347          |
| France <sup>2</sup>                  | 132  | 101                            | 306  | 16                          | (62)           | 493            |
| Germany                              |  | 20                             | 54   | 27                          | 2              | 103            |
| Malta                                | 19   | 23                             | 16   |                             |                | 58             |
| Switzerland                          |  |                                |  | 169                         |                | 169            |
| Turkey                               | 71   | 27                             | 22   |                             |                | 120            |
| Other                                | 61   | 54                             | 142  | 70                          | (17)           | 310            |
|                                      | <b>912</b>                                 | <b>1,076</b>                   | <b>1,202</b>   | <b>388</b>                  | <b>22</b>      | <b>3,600</b>   |
| <b>Half-year to 31 December 2006</b> |  |                                |  |                             |                |                |
| United Kingdom                       | 867  | 950                            | 637  | 274                         | (284)          | 2,444          |
| France <sup>2</sup>                  | 42   | 135                            | 239  | 6                           | (45)           | 377            |
| Germany                              |  | 9                              | 60   | 14                          | 14             | 97             |
| Malta                                | 23   | 27                             | 13   |                             |                | 63             |
| Switzerland                          |  |                                |  | 136                         |                | 136            |
| Turkey                               | 50   | 23                             | 42   |                             | (18)           | 97             |
| Other                                | 15   | 14                             | 111  | (13)                        | 33             | 160            |
|                                      | <b>997</b>                                 | <b>1,158</b>                   | <b>1,102</b>   | <b>417</b>                  | <b>(300)</b>   | <b>3,374</b>   |

Loans and advances to customers (net) by country

|  | Half-year to    |                 |                        |
|--|-----------------|-----------------|------------------------|
|  | 30 June<br>2007 | 30 June<br>2006 | 31<br>December<br>2006 |



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|                | US\$m          | US\$m   | US\$m   |
|----------------|----------------|---------|---------|
| United Kingdom | <b>325,199</b> | 277,077 | 305,758 |
| France2        | <b>67,670</b>  | 54,023  | 55,491  |
| Germany        | <b>5,763</b>   | 4,459   | 4,439   |
| Malta          | <b>3,700</b>   | 3,203   | 3,456   |
| Switzerland    | <b>11,164</b>  | 8,363   | 9,151   |
| Turkey         | <b>6,148</b>   | 4,445   | 5,233   |
| Other          | <b>8,464</b>   | 7,829   | 8,971   |
|                | <b>428,108</b> | 359,399 | 392,499 |

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HSBC HOLDINGS PLC

**Business Review** (continued)

## Customer accounts by country

|                     | Half-year to             |                          |                                 |
|---------------------|--------------------------|--------------------------|---------------------------------|
|                     | 30 June<br>2007<br>US\$m | 30 June<br>2006<br>US\$m | 31<br>December<br>2006<br>US\$m |
| United Kingdom      | 346,547                  | 290,050                  | 318,614                         |
| France <sup>2</sup> | 48,961                   | 47,024                   | 43,372                          |
| Germany             | 9,671                    | 10,915                   | 11,607                          |
| Malta               | 4,779                    | 4,192                    | 4,529                           |
| Switzerland         | 35,266                   | 29,993                   | 30,062                          |
| Turkey              | 5,074                    | 4,291                    | 4,140                           |
| Other               | 8,210                    | 6,268                    | 7,041                           |
|                     | <b>458,508</b>           | <b>392,733</b>           | <b>419,365</b>                  |

1 Including venture capital gains of US\$548 million in the first half of 2007 (US\$117 million in the first half of 2006: US\$340 million in the second half of 2006).

2 France primarily comprises the domestic operations of HSBC France and the Paris branch of HSBC Bank plc.

## Economic briefing

The **UK** economy remained robust throughout the first half of 2007. The growth in gross domestic product ( GDP ) in the first half of the year was 3 per cent year-on-year, broadly in line with its average during the past decade. Consumer spending was relatively strong in the first quarter but slowed in the second as retail spending weakened in response to increases in interest rates. The Bank of England raised the bank rate by 25 basis points in each of January, May and July 2007 to 5.75 per cent. These interest rate rises appeared to restrain housing market activity and subdue house price inflation. However, inflation continued to cause concern as the Consumer Price Index ( CPI ) reached 3.1 per cent, the highest level in ten years, and the Retail Price Index ( RPI ), which includes the cost of housing and mortgage payments, reached 4.8 per cent in March. By June, CPI inflation had eased to 2.4 per cent and RPI inflation to 4.4 per cent. The unemployment rate has remained stable at 5.5 per cent since the middle of 2006.

Having expanded by 2.9 per cent in 2006, GDP in the **eurozone** continued to grow by 3.1 per cent year-on-year in the first quarter of 2007, driven primarily by exports and investment. Employment growth remained robust, allowing the unemployment rate to fall to just 7 per cent, down from 7.5 per cent at the end of 2006. Consumer spending growth remained relatively subdued, primarily due to a 3 percentage point increase in German VAT which took effect in January. French GDP growth remained below the eurozone average at 1.9 per cent in the first quarter of 2007. Eurozone consumer price inflation stayed below 2 per cent throughout the first half of the year as the European Central Bank responded to the robust growth by tightening monetary policy in March and June 2007, taking the repo rate to 4 per cent.

Domestic demand continued to slow in **Turkey** as growth in private consumption, which accounts for nearly two-thirds of the economy, fell to just 1.6 per cent year-on-year in the first quarter of 2007 from 8.1 per cent in 2006. Investment demand growth also plunged to 3 per cent from above 30 per cent in the first quarter of 2006. Despite this, neither inflation nor the current account deficit improved as much as expected. Annual inflation was 8.6 per cent in June (compared with an official target of 4 per cent), partly because of higher food and energy prices. The unemployment rate was also unchanged at 9.8 per cent in April compared with 9.9 per cent a year ago, largely reflecting productivity growth and a shift from agricultural to service sector employment. Although the large interest rate differential kept the Turkish lira strong, monetary policy

remained tight and cautious, with policy rates kept at 17.5 per cent since June 2006 due to high inflation.

#### Review of business performance

European operations reported a pre-tax profit of US\$4,050 million compared with US\$3,600 million in the first half of 2006, an increase of 13 per cent. On an underlying basis, pre-tax profits improved by 3 per cent. The difference was partly attributable to HSBC's acquisition of its partner's shares in life insurer, Erisa S.A., and property and casualty insurer, Erisa I.A.R.D., (together Erisa) in France in March 2007. Underlying revenue growth of 8 per cent was partly offset by higher loan impairment charges and a 10 per cent increase in operating expenses. CIBM delivered the strongest growth in pre-tax profits on the back of trading performance and significant private equity gains. Commercial Banking increased revenues from strong balance sheet growth, improved cross-sales in the UK and ongoing business expansion in Turkey. Private Banking

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## Profit before tax

|   | Half-year to             |                          |                              |
|---|--------------------------|--------------------------|------------------------------|
|   | 30 June<br>2007<br>US\$m | 30 June<br>2006<br>US\$m | 31 December<br>2006<br>US\$m |
| <b>Europe</b>   |                          |                          |                              |
| Net interest income   | 3,920                    | 4,094                    | 4,195                        |
| Net fee income  | 4,144                    | 3,513                    | 3,595                        |
| Net trading income  | 3,338                    | 2,187                    | 2,342                        |
| Net income from financial instruments designated at fair value                              | 348                      | 129                      | 15                           |
| Gains less losses from financial investments  | 790                      | 266                      | 358                          |
| Dividend income   | 161                      | 121                      | 62                           |
| Net earned insurance premiums   | 1,480                    | 668                      | 630                          |
| Other operating income  | 262                      | 633                      | 795                          |
| <b>Total operating income</b>   | <b>14,443</b>            | <b>11,611</b>            | <b>11,992</b>                |
| Net insurance claims incurred and movement in policyholders' liabilities                    | (1,146)                  | (287)                    | (244)                        |
| <b>Net operating income before loan impairment charges and other credit risk provisions</b> | <b>13,297</b>            | <b>11,324</b>            | <b>11,748</b>                |
| Loan impairment charges and other credit risk provisions                                    | (1,363)                  | (935)                    | (1,220)                      |
| <b>Net operating income</b>   | <b>11,934</b>            | <b>10,389</b>            | <b>10,528</b>                |
| Total operating expenses  | (7,972)                  | (6,723)                  | (7,148)                      |
| <b>Operating profit</b>   | <b>3,962</b>             | <b>3,666</b>             | <b>3,380</b>                 |
| Share of (loss)/profit in associates and joint ventures                                     | 88                       | (66)                     | (6)                          |
| <b>Profit before tax</b>  | <b>4,050</b>             | <b>3,600</b>             | <b>3,374</b>                 |
|   | %                        | %                        | %                            |
| Share of HSBC's profit before tax   | 28.6                     | 28.8                     | 35.3                         |
| Cost efficiency ratio   | 60.0                     | 59.4                     | 60.8                         |
| Period-end staff numbers (full-time equivalent)   | 80,912                   | 77,736                   | 78,311                       |

Balance sheet data<sup>1</sup>

|  | US\$m     | US\$m   | US\$m   |
|--|-----------|---------|---------|
| Loans and advances to customers (net)  | 428,108   | 359,399 | 392,499 |
| Loans and advances to banks (net)  | 79,817    | 64,564  | 76,830  |
| Trading assets, financial instruments designated at fair value and financial investments | 370,193   | 230,035 | 242,010 |
| Total assets   | 1,040,019 | 767,608 | 828,701 |
| Deposits by banks  | 86,912    | 55,783  | 67,821  |
| Customer accounts  | 458,508   | 392,733 | 419,365 |

1 Third party only.

performance was notable, as strong demand for wealth management services and increased cross-referrals from HSBC businesses drove growth. In Personal Financial Services, profit before tax was lower than in the first half of 2006 as the benefit of growth in the customer base across the region was offset by a restricted appetite for credit, higher loan impairment charges, and the impact of overdraft fee refunds which increased in the wake of strong media campaigns.

The following commentary is on an underlying basis.

**Personal Financial Services** reported a pre-tax profit of US\$604 million, a decrease of 42 per cent

compared with the first half of 2006. Notwithstanding the fact that income grew at a slower rate than costs, HSBC continued with major initiatives to enhance channel capacity and capabilities in the UK, in addition to pursuing business expansion-related investments across the rest of the region. In the UK, the benefits of targeted balance sheet growth, in particular from packaged accounts and savings products, were more than offset by higher loan impairment charges. In Turkey, pre-tax profits remained unchanged at US\$71 million as the increased costs incurred to support future business growth offset income growth from strong customer acquisition and higher balances. In France, the positive effect on income of

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HSBC HOLDINGS PLC

## Business Review (continued)

customer acquisition and improved transactional commissions, driven by successful marketing campaigns, was offset by narrowing spreads, higher costs, and the non-recurrence of a large benefit in the first half of 2006 from the fair value effect of embedded options linked to government-regulated home savings products.

In the UK, HSBC continued to concentrate on acquiring and retaining customers through innovative services, improved e-sales offerings and a segmented approach to product development. The success of packaged current accounts, the introduction of initiatives to target the affluent, nearly-retired population, and the launch of the MyMoney product, underlined the Group's developing customer segmentation. Channel capacity and capabilities were enhanced through the ongoing retail refurbishment programme and the opening of more non-branch automated teller machines ( ATMs ) and Express Banking kiosks across the country. HSBC Premier, designed to provide seamless cross-border banking, was relaunched in the UK and a further 34 countries.

In France, successful marketing campaigns continued to grow customer numbers. Average lending balances grew significantly, largely driven by mortgages originated in 2006. Sales of new mortgages eased in line with the slowing French housing market.

In Turkey, brand awareness and geographic coverage were enhanced by the opening of 25 branches during the first half of 2007, supported by a number of marketing initiatives. The focus on customer segmentation and cross-sales was aided by the introduction of new banking propositions for low and medium income groups.

Net interest income increased by 2 per cent to US\$3,130 million, substantially in the UK, where HSBC continued to moderate lending growth in favour of competitive deposit products. Net interest income grew steadily, driven by growth in savings and current account balances and wider deposit spreads in the rising interest rate environment. This was partly offset by lower interest income from mortgages as margins narrowed, owing to a change in mix from variable to fixed rate products.

Average unsecured lending balances in the UK declined by 3 per cent as HSBC applied tighter underwriting criteria and emphasised non-lending related revenue streams, reflecting the Group's reduced appetite for risk. Spreads improved slightly, despite the continuing shift in product mix towards higher value, lower yielding loans.

In a highly competitive environment, targeted marketing initiatives helped to boost UK savings account sales by 6 per cent. Average balances reached US\$83 billion, an increase of 14 per cent from 30 June 2006 which, together with improved spreads, contributed to a 33 per cent increase in net interest income. HSBC had the highest market share of new savings account openings in the UK as at May 2007, driven by competitive internet-based products and rates.

Average current account balances in the UK increased by 4 per cent to US\$28 billion. By creating value in its current accounts through the segmented approach to developing customer propositions referred to above, sales of HSBC's premium service current accounts ( Premier and Plus ) increased substantially.

HSBC grew its UK credit card balances by 6 per cent despite the continuing slowdown in the market, although tightening spreads eroded the resulting benefits. Balance growth was strongest in Marks & Spencer ( M&S ) branded cards. HSBC had 18 per cent of the market in terms of credit card sales turnover in the UK at May 2007, with online sales representing 27 per cent of total new account openings for HSBC and First Direct branded cards.

Average mortgage balances rose modestly as HSBC continued to restrict originations to its owned channels and the strongest growth in the market was seen through mortgage brokers. The portfolio mix shifted towards a higher proportion of fixed rate products as customers sought to fix their monthly payments and spreads tightened following the four base rate increases between August 2006 and 30 June 2007. The Group's commitment to providing the best value to its customers was endorsed by *What Mortgage* awarding HSBC Best Value National Bank for the sixth year running.

In France, net interest income fell by 10 per cent. Average lending balances grew by 20 per cent, mainly from mortgages originated in 2006, although the associated income benefits were offset by tightening spreads due to competitive pressure. Increased income from the investment of

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increased interest free deposit balances was negated by maturing higher yielding hedging products.

In Turkey, increased income from strong growth in customer accounts, lending and deposit balances was offset by lower income from credit cards as balance growth and margins were adversely affected by market-wide credit calming measures introduced in 2006. Net interest income stayed broadly in line with the first half of 2006. HSBC made good progress in its plan to add 400,000 new personal

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customers during 2007. Overall, average deposit balances grew by 27 per cent, largely driven by the strong customer recruitment. This was aided by the opening of 37 new branches since 30 June 2006 and ongoing efforts to build brand awareness. Deposit spreads were stable in an environment of rising interest rates. Average lending balances grew by 28 per cent, although the benefits from lending growth were more than offset by compressed margins due to the credit calming measures referred to above, as well as increased competition in the market.

Net fee income increased by 9 per cent, largely driven by higher sales of fee-earning packaged current accounts in the UK and credit cards in Turkey. This was partly offset by a US\$23 million decrease in credit card default fees as HSBC reduced its credit card default fee to £12 following the outcome of an investigation by the UK Office of Fair Trading ( OFT ) in April 2006. In France, improved transactional commissions, mainly from increased demand for packaged accounts and higher life insurance fees drove a 7 per cent increase in fee income.

Net trading income largely reflects the fair value measurement of embedded options linked to government regulated home savings products in France. In 2006, there was a large gain; this did not recur in the first half of 2007.

Gains on sale of financial investments declined due to the non-recurrence of the US\$32 million share of profits from the MasterCard Incorporated IPO in the first half of 2006.

Other operating income declined significantly due to a reduction in the present value of in-force long-term insurance business, reflecting changes in Financial Services Authority ( FSA ) rules. This was more than offset by a decrease in insurance claims. The non-recurrence of Personal Financial Services US\$37 million share of the gain on the sale of HSBC's stake in The Cyprus Popular Bank also contributed to the fall in other operating income, although this was largely offset by Personal Financial Services US\$32 million share of a gain from the merger of two payment services providers.

Loan impairment charges and other credit risk provisions of US\$1,127 million were 24 per cent higher than in the first half of 2006. In the UK, rising trends in personal bankruptcies and IVAs and growth in credit card lending contributed to the increase in charges, as did refinements to the methodology used to calculate roll rate percentages in the UK consumer finance business. Otherwise, overall credit quality was broadly stable. In France

and Turkey, loan impairment charges improved and credit quality also remained sound.

Operating expenses increased by 12 per cent. Within this, US\$236 million reflected goodwill payments expensed in respect of overdraft fees applied in previous years. These payments were made on an ex gratia basis, without any admission of liability, taking into consideration the cost implications of legal action and the reluctance of HSBC Bank to engage in legal action against its customers.

The payments were made during a period in which the OFT and the British Bankers' Association concluded a collaborative informal fact-finding exercise on the legal principles that apply to charges for unauthorised overdrafts, and the OFT announced on 29 March 2007 that it would undertake a formal investigation into the fairness of certain bank current account charges. This investigation remains ongoing and, against this background, came the further announcement on 26 July 2007 that the OFT would, by agreement, issue High Court legal proceedings on 27 July 2007 against a number of UK financial institutions, including HSBC Bank, to determine the legal status and enforceability of these charges.

The roll-out of the UK branch refurbishment programme to a further 26 branches, the opening of four megastores, and the recruitment of additional staff ahead of the introduction of extended opening hours in certain branches were the other significant reasons for the cost increase. In France, operating expenses rose as HSBC made further investments in pursuing its five-year expansion strategy. The 18 per cent increase in operating expenses in Turkey reflected ongoing investment in capacity and infrastructure to support business expansion.

**Commercial Banking** reported a pre-tax profit of US\$1,236 million, an increase of 5 per cent. Revenues rose by 12 per cent as a result of balance sheet growth driven by customer recruitment and improved cross-sales in the UK, and the expansion of the small and mid-market segments in Turkey, Spain and Malta. Credit quality remained relatively good compared with historical experience but there were higher loan impairment charges on corporate relationship managed accounts in the UK and these, along with increased operating expenses from ongoing business expansion throughout the region, largely offset the revenue benefits from balance sheet growth.

HSBC began to expand the scope of its services in European emerging markets. In Poland, the Group extended its Commercial Banking presence to five cities and it recruited more relationship managers in





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Slovakia and the Czech Republic. In May 2007, the Group secured a retail banking licence in Russia, where Commercial Banking services are focused on mid-market corporate clients with international trade requirements. HSBC also continued to develop its receivables finance offering with operations launched in Greece, Malta and Turkey in the first half of 2007.

In the UK, profit before tax increased by 7 per cent as HSBC placed considerable emphasis on increasing sales capacity through the recruitment of sales staff and investment in direct channels. The number of active customers on the Business Internet Banking platform increased by over 36 per cent with log-ons increasing by 20 per cent compared with the first half of 2006. Business Direct, HSBC's commercial direct banking proposition, launched in September 2006, attracted over 22,000 new accounts, more than doubling account numbers on this channel, of which over 70 per cent were opened by new customers to HSBC. Physical infrastructure was enhanced to improve customer experience. The International Banking Centre, which was opened in 2006 to support the Group's drive to lead the market in international commercial banking, continued to streamline cross-border account openings. Commercial Centres within the distribution network were refurbished, and business zones focused on small business customers were installed within retail branches.

Net interest income increased by 10 per cent in the first half of 2007, largely from growth in the UK, Turkey, Germany and Malta. In the UK, a 9 per cent growth in deposit balances helped fund lending growth of 14 per cent. Libor-linked loan balances increased by over 50 per cent, with business loans and commercial mortgages up by 8 per cent and 24 per cent, respectively.

In France, higher net interest income derived from 18 per cent increases in both loan balances and deposit balances did not fully compensate for lower income from the placement of interest-free current account balances and tighter spreads on lending products. Customer recruitment remained buoyant as ongoing efforts to enhance brand awareness and improve segmentation among commercial business customers met with success.

Net interest income in Turkey increased by 47 per cent, as HSBC continued to develop its service offerings for its micro-, small- and medium-sized business customers. Lending growth of 32 per cent delivered a strong rise in income despite tighter spreads resulting from increased competition. Average deposit balances rose by 8 per cent, with

wider margins augmenting the benefits from balance growth.

Excluding Commercial Banking's US\$97 million share of Insurance Brokers' fees previously included in the Other segment (see page 18), net fee income increased by 5 per cent. In the UK, a modest increase in net fee income was driven by strong performance in foreign exchange products, although growth was constrained by a structural shift from paper to electronic money transactions and reduced reliance on banks to facilitate overseas trade payments in an evolving trade finance environment. Bill and BACS payments made using internet banking increased by 33 per cent on the first half of 2006. In Turkey, net fee income grew by 78 per cent, driven by investment banking, advisory and structured finance transactions. In France, net fee income grew by 4 per cent as transaction fees increased.

Other operating income declined significantly, due to a reduction in the present value of in-force long-term insurance business, reflecting changes in FSA rules. This was more than offset by a decrease in insurance claims. The non-recurrence of Commercial Banking's US\$38 million share of the gain on the sale of HSBC's stake in The Cyprus Popular Bank Limited (Cyprus Popular Bank) also contributed to the fall in other operating income.

Loan impairment charges and other credit risk provisions remained low despite a 61 per cent rise compared with levels recorded in the first half of 2006. In the UK, loan impairment charges increased, reflecting provisions against bad debts due from two large corporate accounts and the ongoing impact of individual voluntary arrangements (IVAs) on the micro business segment. In France, loan impairment charges were in line with the first half of 2006 while, in Turkey, increased charges reflected growth in lending volumes as general credit quality remained satisfactory.

Excluding Commercial Banking's US\$122 million share of Insurance Brokers' expenses referred to above, operating expenses increased by 2 per cent, less than revenue growth of 7 per cent. Across Europe, growth in operating expenses primarily resulted from the recruitment of additional sales staff and other costs incurred in support of the growing business. Additionally, in France, there were incremental expenses associated with

the merger of four regional banking subsidiaries.

**Corporate, Investment Banking and Markets** in Europe reported a pre-tax profit of US\$1,674 million, which represented 40 per cent of the global

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business's pre-tax profits, and a rise of 27 per cent compared with the first half of 2006. Increased trading revenues, significant gains from the private equity business and higher Global Banking fees resulted in an improvement in the cost efficiency ratio of 1.7 percentage points.

Total operating income increased by 19 per cent to US\$4,170 million. In the UK, balance sheet management revenues decreased by 63 per cent as higher short-term interest rates resulted in a reduction in margins. Net interest income from corporate lending declined due to lower credit spreads in a competitive market.

Payments and cash management revenues increased due to steady balance growth, primarily driven by higher volumes from institutional customers.

Net fee income rose by 28 per cent, within which financing fees increased strongly due to a notable expansion in syndicated transaction volumes generated by HSBC's leveraged and acquisition finance business.

Increased income from securities services reflected growth in assets under administration and custody, which rose by 30 per cent and 19 per cent, respectively, from a rise in business volumes, an increase in new clients and higher market values.

Income from trading activities also increased, largely in the areas of structured derivatives and equities. Structured derivatives reported a 44 per cent rise, reflecting success in delivering risk management and investment solutions. HSBC benefited from recognising income deferred in previous periods as markets became more liquid and price transparency improved on more complex products. Excluding a US\$93 million gain from the disposal of shares in Euronext N.V., revenues in the equities business rose by 87 per cent, led by a strong performance in equity financing and cash equities in the buoyant market environment. Foreign exchange revenues were broadly in line with last year.

Gains from sales of financial investments increased threefold to US\$651 million, primarily due to successful private equity disposals in the UK and France.

A net recovery on loan impairment charges, albeit lower than that reported in the first half of 2006, reflected the continuation of the benign corporate credit environment.

Operating expenses rose by 16 per cent to US\$2,513 million, with the growth in expenses being lower than revenue growth. In Global Markets, increased volumes, particularly in structured derivatives, led to a modest rise in staff numbers. Higher profitability resulted in increased performance-related costs.

HSBC's share of profits from associates improved significantly, due to the non-recurrence of an impairment charge on a private equity investment held by an associate in the first half of 2006.

**Private Banking** continued to deliver robust growth, reporting profit before tax of US\$493 million, 23 per cent higher than in the first half of 2006. The cost efficiency ratio of 52.5 per cent was 4.3 percentage points better than a year ago. Particularly good performances were recorded in the UK and Monaco, where the entrepreneurial client bases were very active in managing their portfolios. There was strong demand for wealth management services, and improved cooperation with other HSBC businesses led to increased cross-referrals. Organic growth more than compensated for a reduction in one-off revenues and an adverse fair value movement on non-qualifying hedges.

Net interest income increased by 10 per cent to US\$365 million, largely due to balance sheet growth. The business in Switzerland was the main contributor to the rise, with an increase in net interest income of 24 per cent, driven by significant growth in loans and advances to customers. In the UK, an increased customer base and interest rate rises contributed to higher net interest income.

Net fee income of US\$523 million was 5 per cent higher than in the first half of 2006, despite the non-recurrence of a US\$36 million performance fee received from the Hermitage Fund in the first half of 2006. Growth was driven by increased funds under management. In Switzerland, client activity was focused upon higher-value structured products and investment in advisory and discretionary portfolios, from which fee income rose by 80 per cent.

Trading income in the first six months of 2007 of US\$87 million was 38 per cent higher than in the first half of 2006. This increase, largely in Switzerland, was driven by elevated levels of private client foreign exchange activity.

Gains from financial investments doubled to US\$42 million. The partial disposal of a seed capital investment in the Hermitage Fund realised gains of US\$23 million. A US\$7 million gain in France on the disposal of securities in the first half of 2006 did not recur in 2007.

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Client assets, which include deposits and funds under management, rose by 8 per cent to US\$237 billion. Net new money of US\$11 billion

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**Business Review** (continued)

was garnered in the first half of 2007, of which US\$7 billion came from Switzerland. Significant inflows of net new money were also generated in Germany and Monaco. The Investment Solutions suite of discretionary managed products continued to attract client investment, with the value of invested assets increasing by 34 per cent since 31 December 2006.

Operating expenses were 3 per cent higher than in the first half of 2006, driven by increased investment in infrastructure and branch expansion in support of business growth. This was largely offset by the effect of a change in pension arrangements.

The results of the HSBC Insurance Brokers group were allocated to HSBC's customer groups in

the first half of 2007, having been reported within **Other** in 2006. As a consequence, net operating income before loan impairment charges and operating expenses were US\$205 million and US\$178 million, respectively, lower than in the first half of 2006, reducing profit before tax by US\$27 million.

HSBC realised US\$70 million from the sale of financial investments in the first half of 2007.

Also included within Other were fair value movements of US\$203 million on HSBC's own debt in issue and related swaps.

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Profit/(loss) before tax and balance sheet data by customer group and global business

Half-year to 30 June 2007

| Europe  | Personal<br>Financial<br>Services<br>US\$m | Commercial<br>Banking<br>US\$m | Corporate,<br>Investment<br>Banking &<br>Markets<br>US\$m | Private<br>Banking<br>US\$m | Other<br>US\$m | Inter-<br>segment<br>elimination<br>US\$m | Total<br>US\$m |
|---|--|--------------------------------|---|-----------------------------|----------------|---|----------------|
| Net interest income   | 3,130                                      | 1,647                          | 495   | 365                         | 32             | (1,749)                                   | 3,920          |
| Net fee income  | 1,428                                      | 1,066                          | 1,108   | 523                         | 19             |   | 4,144          |
| Trading income/(expense)<br>excluding net interest<br>income  | 45   | 11                             | 1,705   | 83                          | (2)            |   | 1,842          |
| Net interest<br>income/(expense) on trading<br>activities   | (2)  | 12                             | (268)   | 4                           | 1              | 1,749                                     | 1,496          |
| Net trading<br>income/(expense)   | 43   | 23                             | 1,437   | 87                          | (1)            | 1,749                                     | 3,338          |
| Net income/(expense) from<br>financial instruments<br>designated at fair value .                        | 315  | 9                              | (2)   |                             | 26             |   | 348            |
| Gains less losses from<br>financial investments   | 19   | 8                              | 651   | 42                          | 70             |   | 790            |
| Dividend income   | 1  | 2                              | 144   | 5                           | 9              |   | 161            |
| Net earned insurance<br>premiums  | 1,380                                      | 109                            |   |                             | (9)            |   | 1,480          |
| Other operating<br>income/(expense)   | (110)                                      | (89)                           | 337   | 9                           | 147            | (32)                                      | 262            |
| <b>Total operating income</b>   | <b>6,206</b>                               | <b>2,775</b>                   | <b>4,170</b>  | <b>1,031</b>                | <b>293</b>     | <b>(32)</b>                               | <b>14,443</b>  |
| Net insurance claims l  | (1,245)                                    | 99                             |   |                             |                |   | (1,146)        |
| <b>Net operating income<br/>before loan impairment<br/>charges and other credit<br/>risk provisions</b> | <b>4,961</b>                               | <b>2,874</b>                   | <b>4,170</b>  | <b>1,031</b>                | <b>293</b>     | <b>(32)</b>                               | <b>13,297</b>  |
| Loan impairment<br>(charges)/recoveries and<br>other credit risk provisions                             | (1,127)                                    | (256)                          | 17  | 3                           |                |   | (1,363)        |
| <b>Net operating income</b>   | <b>3,834</b>                               | <b>2,618</b>                   | <b>4,187</b>  | <b>1,034</b>                | <b>293</b>     | <b>(32)</b>                               | <b>11,934</b>  |
| Total operating expenses  | (3,244)                                    | (1,382)                        | (2,513)   | (541)                       | (324)          | 32  | (7,972)        |
| <b>Operating profit/(loss)</b>  | <b>590</b>                                 | <b>1,236</b>                   | <b>1,674</b>  | <b>493</b>                  | <b>(31)</b>    |   | <b>3,962</b>   |
| Share of profit in associates<br>and joint ventures   | 14   |                                |   |                             | 74             |   | 88             |
| <b>Profit before tax</b>  | <b>604</b>                                 | <b>1,236</b>                   | <b>1,674</b>  | <b>493</b>                  | <b>43</b>      |   | <b>4,050</b>   |
|   | %  | %                              | %   | %                           | %              |   | %              |
| Share of HSBC s profit<br>before tax  | 4.3  | 8.7                            | 11.8  | 3.5                         | 0.3            |   | 28.6           |

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|                       |             |             |             |             |              |             |
|-----------------------|-------------|-------------|-------------|-------------|--------------|-------------|
| Cost efficiency ratio | <b>65.4</b> | <b>48.1</b> | <b>60.3</b> | <b>52.5</b> | <b>110.6</b> | <b>60.0</b> |
|-----------------------|-------------|-------------|-------------|-------------|--------------|-------------|

**Balance sheet data<sup>2</sup>**

|  | <b>US\$m</b>   | <b>US\$m</b>   | <b>US\$m</b>   | <b>US\$m</b>  | <b>US\$m</b> | <b>US\$m</b>     |
|--|----------------|----------------|----------------|---------------|--------------|------------------|
| Loans and advances to customers (net)  | <b>149,789</b> | <b>87,247</b>  | <b>165,028</b> | <b>25,544</b> | <b>500</b>   | <b>428,108</b>   |
| Total assets   | <b>198,518</b> | <b>104,420</b> | <b>677,459</b> | <b>56,090</b> | <b>3,532</b> | <b>1,040,019</b> |
| Customer accounts  | <b>166,282</b> | <b>83,421</b>  | <b>153,196</b> | <b>54,893</b> | <b>716</b>   | <b>458,508</b>   |
| Loans and advances to banks (net) <sup>3</sup>   |                |                | <b>66,281</b>  |               |              |                  |
| Trading assets, financial instruments designated at fair value, and financial investments <sup>3</sup> |                |                | <b>322,862</b> |               |              |                  |
| Deposits by banks <sup>3</sup>   |                |                | <b>85,104</b>  |               |              |                  |

*For footnotes, see page 33.*



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**Business Review** (continued)

Profit/(loss) before tax and balance sheet data by customer group and global business (continued)

|  | Half-year to 30 June 2006                  |                                |   |                             |                |   |                |
|--|--|--------------------------------|---|-----------------------------|----------------|---|----------------|
| <b>Europe</b>  | Personal<br>Financial<br>Services<br>US\$m | Commercial<br>Banking<br>US\$m | Corporate,<br>Investment<br>Banking &<br>Markets<br>US\$m | Private<br>Banking<br>US\$m | Other<br>US\$m | Inter-<br>segment<br>elimination<br>US\$m | Total<br>US\$m |
| Net interest income  | 2,711                                      | 1,367                          | 429   | 322                         | 20             | (755)                                     | 4,094          |
| Net fee income   | 1,230                                      | 845                            | 796   | 482                         | 160            |   | 3,513          |
| Trading income excluding net<br>interest income  | 100  | 5                              | 1,373   | 54                          | 15             |   | 1,547          |
| Net interest income/(expense)<br>on trading activities                                     |  | 2                              | (124)   | 7                           |                | 755                                       | 640            |
| Net trading income   | 100  | 7                              | 1,249   | 61                          | 15             | 755                                       | 2,187          |
| Net income from financial<br>instruments designated at fair<br>value                       | 11   | 1                              | 4   |                             | 113            |   | 129            |
| Gains less losses from financial<br>investments  | 32   | 12                             | 198   | 20                          | 4              |   | 266            |
| Dividend income  |  | 2                              | 113   | 4                           | 2              |   | 121            |
| Net earned insurance premiums  | 461  | 60                             |   |                             | 147            |   | 668            |
| Other operating income   | 61   | 58                             | 416   | 5                           | 139            | (46)                                      | 633            |
| <b>Total operating income</b>  | <b>4,606</b>                               | <b>2,352</b>                   | <b>3,205</b>  | <b>894</b>                  | <b>600</b>     | <b>(46)</b>                               | <b>11,611</b>  |
| Net insurance claims <sup>1</sup>  | (181)                                      | (5)                            |   |                             | (101)          |   | (287)          |
| Net operating income before<br>loan impairment charges and<br>other credit risk provisions | 4,425                                      | 2,347                          | 3,205   | 894                         | 499            | (46)                                      | 11,324         |
| Loan impairment<br>(charges)/recoveries and other<br>credit risk provisions                | (847)                                      | (145)                          | 56  | 1                           |                |   | (935)          |
| <b>Net operating income</b>  | <b>3,578</b>                               | <b>2,202</b>                   | <b>3,261</b>  | <b>895</b>                  | <b>499</b>     | <b>(46)</b>                               | <b>10,389</b>  |
| Total operating expenses   | (2,666)                                    | (1,126)                        | (1,989)   | (507)                       | (481)          | 46  | (6,723)        |
| Operating profit   | 912  | 1,076                          | 1,272   | 388                         | 18             |   | 3,666          |
| Share of profit/(loss) in<br>associates and joint ventures                                 |  |                                | (70)  |                             | 4              |   | (66)           |
| <b>Profit before tax</b>   | <b>912</b>                                 | <b>1,076</b>                   | <b>1,202</b>  | <b>388</b>                  | <b>22</b>      |   | <b>3,600</b>   |

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|                                   | %    | %    | %    | %    | %    | %    |
|-----------------------------------|------|------|------|------|------|------|
| Share of HSBC's profit before tax | 7.3  | 8.6  | 9.6  | 3.1  | 0.2  | 28.8 |
| Cost efficiency ratio             | 60.2 | 48.0 | 62.1 | 56.7 | 96.4 | 59.4 |

Balance sheet data<sup>2</sup>

|  | US\$m   | US\$m  | US\$m   | US\$m  | US\$m | US\$m   |
|--|---------|--------|---------|--------|-------|---------|
| Loans and advances to customers (net)  | 132,064 | 71,357 | 134,892 | 21,085 | 1     | 359,399 |
| Total assets   | 157,214 | 85,445 | 475,006 | 45,739 | 4,204 | 767,608 |
| Customer accounts  | 140,210 | 69,322 | 136,695 | 46,506 |       | 392,733 |
| Loans and advances to banks (net) <sup>3</sup>   |         |        | 53,280  |        |       |         |
| Trading assets, financial instruments designated at fair value, and financial investments <sup>3</sup> |         |        | 207,563 |        |       |         |
| Deposits by banks <sup>3</sup>   |         |        | 53,711  |        |       |         |

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Half-year to 31 December 2006

| <b>Europe</b>  | Personal<br>Financial<br>Services<br>US\$m | Commercial<br>Banking<br>US\$m | Corporate,<br>Investment<br>Banking &<br>Markets<br>US\$m | Private<br>Banking<br>US\$m | Other<br>US\$m | Inter-<br>segment<br>elimination<br>US\$m | Total<br>US\$m |
|--|--|--------------------------------|---|-----------------------------|----------------|---|----------------|
| Net interest income/(expense)  | 2,942                                      | 1,556                          | 793   | 353                         | (6)            | (1,443)                                   | 4,195          |
| Net fee income   | 1,303                                      | 862                            | 877   | 387                         | 166            |   | 3,595          |
| Trading income/(expense)<br>excluding net interest income                                  | 19   | 22                             | 1,263   | 45                          | (54)           |   | 1,295          |
| Net interest income/(expense)<br>on trading activities                                     | (6)  | 13                             | (399)   | (5)                         | 1              | 1,443                                     | 1,047          |
| Net trading income/(expense)   | 13   | 35                             | 864   | 40                          | (53)           | 1,443                                     | 2,342          |
| Net income/(expense) from<br>financial instruments<br>designated at fair value             | 69   | 26                             | 7   |                             | (87)           |   | 15             |
| Gains less losses from financial<br>investments  | 5  | 10                             | 215   | 129                         | (1)            |   | 358            |
| Dividend income  | 2  | 1                              | 58  | 1                           |                |   | 62             |
| Net earned insurance premiums  | 518  | 50                             |   |                             | 62             |   | 630            |
| Other operating income   | 67   | 45                             | 541   | 8                           | 117            | 17  | 795            |
| <b>Total operating income</b>  | <b>4,919</b>                               | <b>2,585</b>                   | <b>3,355</b>  | <b>918</b>                  | <b>198</b>     | <b>17</b>                                 | <b>11,992</b>  |
| Net insurance claims <sup>1</sup>  | (150)                                      | (14)                           |   |                             | (80)           |   | (244)          |
| Net operating income before<br>loan impairment charges and<br>other credit risk provisions | 4,769                                      | 2,571                          | 3,355   | 918                         | 118            | 17  | 11,748         |
| Loan impairment<br>(charges)/recoveries and other<br>credit risk provisions                | (991)                                      | (241)                          | 8   | 1                           | 3              |   | (1,220)        |
| <b>Net operating income</b>  | <b>3,778</b>                               | <b>2,330</b>                   | <b>3,363</b>  | <b>919</b>                  | <b>121</b>     | <b>17</b>                                 | <b>10,528</b>  |
| <b>Total operating expenses</b>  | <b>(2,781)</b>                             | <b>(1,172)</b>                 | <b>(2,235)</b>  | <b>(503)</b>                | <b>(440)</b>   | <b>(17)</b>                               | <b>(7,148)</b> |
| <b>Operating profit/(loss)</b>   | <b>997</b>                                 | <b>1,158</b>                   | <b>1,128</b>  | <b>416</b>                  | <b>(319)</b>   |   | <b>3,380</b>   |
| Share of profit/(loss) in<br>associates and joint ventures                                 |  |                                | (26)  | 1                           | 19             |   | (6)            |
| <b>Profit/(loss) before tax</b>  | <b>997</b>                                 | <b>1,158</b>                   | <b>1,102</b>  | <b>417</b>                  | <b>(300)</b>   |   | <b>3,374</b>   |
|  | %  | %                              | %   | %                           | %              |   | %              |
| Share of HSBC's profit before<br>tax   | 10.4                                       | 12.1                           | 11.5  | 4.4                         | (3.1)          |   | 35.3           |
| Cost efficiency ratio  | 58.3                                       | 45.6                           | 66.6  | 54.8                        | 372.9          |   | 60.8           |
| <b>Balance sheet data<sup>2</sup></b>  |  |                                |   |                             |                |   |                |
|  | US\$m                                      | US\$m                          | US\$m   | US\$m                       | US\$m          |   | US\$m          |
| Loans and advances to<br>customers (net)   | 147,507                                    | 81,430                         | 140,277   | 23,283                      | 2              |   | 392,499        |

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|   |         |        |         |        |       |         |
|---|---------|--------|---------|--------|-------|---------|
| Total assets  | 174,865 | 98,073 | 502,340 | 49,440 | 3,983 | 828,701 |
| Customer accounts   | 152,411 | 80,312 | 139,416 | 47,223 | 3     | 419,365 |
| Loans and advances to banks<br>(net) <sup>3</sup>   |         |        | 63,788  |        |       |         |
| Trading assets, financial<br>instruments designated at fair<br>value, and financial<br>investments <sup>3</sup> |         |        | 219,304 |        |       |         |
| Deposits by banks <sup>3</sup>  |         |        | 65,963  |        |       |         |

1 *Net insurance claims incurred and movement in policyholders' liabilities.*

2 *Third party only.*

3 *These assets and liabilities were significant to Corporate, Investment Banking and Markets.*

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HSBC HOLDINGS PLC

**Business Review** (continued)**Hong Kong**

Profit/(loss) before tax by customer group and global business

|   | Half-year to             |                          |                                 |
|---|--------------------------|--------------------------|---------------------------------|
|   | 30 June<br>2007<br>US\$m | 30 June<br>2006<br>US\$m | 31<br>December<br>2006<br>US\$m |
| Personal Financial Services               | 1,898                    | 1,420                    | 1,460                           |
| Commercial Banking                        | 760                      | 587                      | 734                             |
| Corporate, Investment Banking and Markets | 697                      | 477                      | 478                             |
| Private Banking                           | 161                      | 123                      | 78                              |
| Other                                     | (186)                    | 47                       | (222)                           |
| <b>Profit before tax</b>                  | <b>3,330</b>             | <b>2,654</b>             | <b>2,528</b>                    |

Profit before tax

|   | Half-year to             |                          |                                 |
|---|--------------------------|--------------------------|---------------------------------|
|   | 30 June<br>2007<br>US\$m | 30 June<br>2006<br>US\$m | 31<br>December<br>2006<br>US\$m |
| Net interest income   | 2,568                    | 2,158                    | 2,527                           |
| Net fee income  | 1,439                    | 1,000                    | 1,056                           |
| Net trading income  | 469                      | 306                      | 311                             |
| Net income from financial instruments designated at fair value                              | 210                      | 6                        | 254                             |
| Gains less losses from financial investments  | 32                       | 122                      | 40                              |
| Dividend income   | 17                       | 59                       | 2                               |
| Net earned insurance premiums   | 1,426                    | 1,317                    | 1,311                           |
| Other operating income  | 413                      | 443                      | 391                             |
| <b>Total operating income</b>   | <b>6,574</b>             | <b>5,411</b>             | <b>5,892</b>                    |
| Net insurance claims incurred and movement in policyholders' liabilities                    | (1,512)                  | (1,193)                  | (1,506)                         |
| <b>Net operating income before loan impairment charges and other credit risk provisions</b> | <b>5,062</b>             | <b>4,218</b>             | <b>4,386</b>                    |
| Loan impairment charges and other credit risk provisions                                    | (80)                     | (70)                     | (102)                           |

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|  |                |         |         |
|--|----------------|---------|---------|
| <b>Net operating income</b>                      | <b>4,982</b>   | 4,148   | 4,284   |
| Total operating expenses                         | <b>(1,665)</b> | (1,504) | (1,765) |
| <b>Operating profit</b>                          | <b>3,317</b>   | 2,644   | 2,519   |
| Share of profit in associates and joint ventures | <b>13</b>      | 10      | 9       |
| <b>Profit before tax</b>                         | <b>3,330</b>   | 2,654   | 2,528   |

|   |               |          |          |
|---|---------------|----------|----------|
|   | <b>%</b>      | <b>%</b> | <b>%</b> |
| Share of HSBC's profit before tax               | <b>23.5</b>   | 21.2     | 26.4     |
| Cost efficiency ratio                           | <b>32.9</b>   | 35.7     | 40.2     |
| Period-end staff numbers (full-time equivalent) | <b>27,066</b> | 26,739   | 27,586   |

Balance sheet data<sup>1</sup>

|   |                |         |         |
|---|----------------|---------|---------|
|   | <b>US\$m</b>   | US\$m   | US\$m   |
| Loans and advances to customers (net)   | <b>89,918</b>  | 86,154  | 84,282  |
| Loans and advances to banks (net)   | <b>68,162</b>  | 45,288  | 50,359  |
| Trading assets, financial instruments designated at fair value, and financial investments | <b>98,998</b>  | 81,109  | 103,734 |
| Total assets  | <b>300,681</b> | 246,781 | 272,428 |
| Deposits by banks   | <b>10,383</b>  | 5,816   | 4,799   |
| Customer accounts   | <b>205,219</b> | 180,167 | 196,691 |

<sup>1</sup> *Third party only.*

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## Economic briefing

**Hong Kong** s economy was robust in the first half of 2007, especially private consumption. Rising wages in the increasingly tight labour market, strong household savings and high asset values supported a sustained expansion of consumer spending which is expected to continue throughout the year. Despite rising wages, headline inflation was low and appeared set to remain so, aided in part by concessionary budget measures. Nevertheless, underlying cost pressures continued to increase. Overall, the property market became more active in the first half of 2007 after stagnating throughout 2006, as increasing levels of private development helped offset a fall in public investment in construction in the absence of large-scale infrastructure projects.

## Review of business performance

HSBC s operations in Hong Kong reported a pre-tax profit of US\$3,330 million compared with US\$2,654 million in the first half of 2006, an increase of 25 per cent. On an underlying basis, pre-tax profits grew by 26 per cent. Underlying net operating income increased by 21 per cent, significantly ahead of operating expenses, which grew by 11 per cent. In CIBM, income growth was driven by a marked improvement in balance sheet management income. In Personal Financial Services and Commercial Banking, balance sheet growth and improved cost efficiency drove a rise in pre-tax profits. Private Banking delivered an excellent performance as a result of strong balance sheet growth and increased demand for investment funds and discretionary products.

The following commentary is on an underlying basis.

**Personal Financial Services** reported a record pre-tax profit of US\$1,898 million, an increase of 35 per cent compared with the first half of 2006. As a result of higher fee income and greater loan and deposit balances, net operating income rose by 28 per cent. This was despite a modest increase in loan impairment charges. Expenses also rose, though continued growth in key customer segments led to increased income and resulted in an improved cost efficiency ratio of 27.6 per cent.

Net interest income grew by 15 per cent to US\$1,588 million as average deposit balances rose. Higher interest rates outside Hong Kong allowed total deposit spreads to widen, driven by spreads on foreign currency accounts. Average customer deposits grew by 9 per cent, benefiting from a series

of promotional campaigns and a competitive pricing strategy.

Stable domestic interest rates in 2007 and an improved economic environment underpinned the domestic property market, which became more active, but intense competition drove down mortgage loan rates. Nevertheless, HSBC continued to rank as one of the leaders in new loan sales, despite aggressive promotional offers and incentives from other banks.

Growth in net interest income was also attributable to a 15 per cent rise in credit card balances, where HSBC remained the market leader. Retailer discount offers, instalment plans and lucky draw programmes stimulated increased customer spending. In addition, a mass acquisition programme brought the number of HSBC cards in circulation to 4.8 million, an increase of 9 per cent since 30 June 2006.

Successful product design and greater use of direct channels combined with strong investment market sentiment to deliver a 68 per cent increase in net fee income, to US\$791 million. Fees from investment products increased by 111 per cent compared with the first half of 2006, as a steady stream of IPOs, inflows of capital and growth in retail participation in mainland China-related shares listed in Hong Kong collectively contributed to a buoyant stock market. Sales of unit trusts and retail securities increased, benefiting from the introduction of new funds, the launch of investment schemes and awareness campaigns, and the phased implementation of WealthMaster , a portfolio wealth management sales tool. Funds under management for investment products maintained a strong growth trend and were 35 per cent greater than at 30 June 2006.

Credit card fee income rose by 23 per cent, as promotional campaigns helped increase the number of cards in circulation and cardholder spending rose by 17 per cent as retail sales remained high.

In the life insurance business, HSBC focused on a suite of retirement planning services and launched simple and innovative investment-linked insurance products. As a result, life premiums increased by 30 per cent. Sales of non-life policies were supported by greater customer use of lower-cost distribution channels. The number of non-life policies sold through direct channels represented a significant percentage of the total policies sold.

Loan impairment charges remained low at US\$74 million, US\$19 million higher than in the first half of 2006. The rise in loan impairment





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HSBC HOLDINGS PLC

## Business Review (continued)

charges primarily reflected increased credit card lending, as the broader credit environment remained relatively benign.

Operating expenses were 13 per cent higher than in the first half of 2006. Branch expansion and refurbishment, and the addition of 9 new branches, resulted in increased premises costs. Staff costs also rose, driven by additional front office staff and performance-related expenses. The cost efficiency ratio improved, however, partly due to the increased use of direct channels.

**Commercial Banking** continued its recent impressive growth with a record pre-tax profit of US\$760 million, 30 per cent higher than in the first half of 2006. Strong liability growth was complemented by the active management of spreads on foreign currency savings in a highly competitive market. Dedicated small business centres and the recruitment of extra staff produced award-winning service and, along with customer-focused product development and active marketing, increased the revenue base. The cost efficiency ratio improved by 2.5 percentage points to 24.5 per cent as revenues grew at a significantly faster rate than costs.

Net interest income increased by 18 per cent, as new accounts and strong demand for savings and time deposit products led to higher average liability balances. While domestic interest rates remained stable following rises in 2006, local currency deposits increased substantially due to strong economic growth and the performance of the stock market in Hong Kong. Foreign currency deposits also increased significantly as global interest rates rose. Promotional activities solidified HSBC's position as the most recommended bank for small and mid-market entities and, in conjunction with an external referral programme, contributed to the opening of more than 16,000 additional BusinessVantage accounts. Call centre sales capabilities were enhanced, facilitating increased sales of packaged products to small and micro businesses.

Total lending facilities increased by 18 per cent. Non-trade lending balances also increased by 18 per cent as the local economy continued to grow and demand for credit remained high. Cross-border lending to manufacturers with operations in mainland China continued to be strong as intra-Asia trade expanded. Asset spreads were generally tighter as a result of market competition, particularly for corporate and mid-market business customers.

Net fee income of US\$250 million was 15 per cent higher than in the first half of 2006. Cash management and remittance fees increased by 9 per cent, driven by rising trade flows and accelerated service times. Demand for investment products was robust as a result of buoyant equity markets in both mainland China and Hong Kong, which were bolstered by the loosening of restrictions in the former on cross-border investments. This generated significant increases in income from unit trusts, structured products and trading income.

Following realignment of the sales force, the Commercial Banking insurance business experienced strong growth, with a 7 per cent rise in insurance fee income. Net earned insurance premiums were 25 per cent higher, but were offset by higher claims.

The business card launched by HSBC in 2006 became Hong Kong's leading such card in the first half of 2007, generating new revenues. The contribution from the commercial card acquiring business fell compared with the first half of 2006, due to the transfer of the card acquiring business to a joint venture with Global Payments Inc. in July 2006.

Loan impairment charges fell sharply by 97 per cent, due to a limited number of new loan impairment charges. Credit quality remained strong despite rising costs faced by manufacturers.

Total expenses rose by 7 per cent, compared with revenue growth of 18 per cent. Direct channels were used for more than a third of all transactions and this contributed to efficiencies that mitigated the increased cost of processing higher volumes. In addition, customers increasingly embraced the commercial-only branches which were launched in 2006 and provide enhanced services at a lower cost than existing branches. Recruitment of sales and insurance staff continued, with over 100 additional staff hired to support expanded insurance operations and product initiatives. Employee costs, including performance-related expenses, rose accordingly, while other expenses remained broadly stable.

**Corporate, Investment Banking and Markets** in Hong Kong reported a pre-tax profit of US\$697 million, which represented 17 per cent of the global business's pre-tax profits, and a rise of 47 per cent compared with the first half of 2006. This was principally due to significant revenue growth in balance sheet management and Global Markets. The cost efficiency ratio improved by 8.3 percentage points.

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Total operating income of US\$1,181 million was 34 per cent higher than in the first half of 2006, as client-driven revenues grew, reflecting the continued expansion of the local economy.

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Net interest income rose significantly, primarily due to a recovery of revenues in balance sheet management. In Global Banking, the rising interest rate environment boosted deposit growth and contributed to an improvement in related margins, partly mitigating continued lending margin compression resulting from strong local competition.

Net fee income increased by 13 per cent, driven by the underlying strength of capital markets. Higher revenues from securities services and debt underwriting activity reflected increased client volumes, encouraged by continuing investor confidence in the buoyant local stock market. This was partially offset by a significant reduction in structured finance fees, the result of lower transaction volumes.

In Group Investment Businesses, robust performance reflected continued growth in domestic markets and strong sales of multi-manager funds.

The rise in net trading income was primarily driven by higher revenues from credit and rates, structured derivatives and equities. The revenue growth was the consequence of greater market volatility and the success of initiatives taken in previous years to extend the product range. Higher customer volumes were achieved as the distribution of CIBM's products to HSBC's personal, private banking and commercial customers increased.

The rise in other operating income reflected higher revenues in the form of expenses incurred in Hong Kong recovered from other regions.

The overall credit environment remained benign with a small loan impairment charge, compared with a net release in 2006.

Operating expenses of US\$474 million rose by 11 per cent, 23 percentage points less than revenue growth. The increase was primarily due to selective investment in Global Markets, particularly in the equities, structured derivatives and securities services. Staff costs rose, due to performance-related costs which increased in line with revenues, and the first full half-year effect of staff recruited in 2006.

**Private Banking** recorded a pre-tax profit of US\$161 million, 32 per cent higher than in the first half of 2006. The cost efficiency ratio improved nearly one percentage point to 40.4 per cent. Strong

balance sheet growth and demand from clients for investment in structured products and investment funds underpinned the impressive performance in the first half of 2007.

Net interest income grew very strongly, rising by 44 per cent to US\$49 million. A substantial increase was recorded in deposit balances following client acquisition and this, together with improved treasury performance in a higher interest rate environment than in the early part of 2006, were the main drivers of the increase in net interest income. Loans and advances to customers were significantly higher than in the corresponding period in 2006, as clients borrowed to fund investment in the equity markets, notably through the use of structured equity products.

The impressive growth in fee income continued, increasing by 38 per cent to US\$80 million. Buoyant stock market performance sustained client demand for structured equity products, including the Forward Accumulator product. In June, HSBC launched the MultiAlpha China Fund, with over one quarter of the US\$1.1 billion raised placed by Private Banking in Hong Kong. The launch of a number of other investment funds and an increase in performance fees received from discretionary managed products also contributed to the overall growth.

Client assets rose by 22 per cent compared with 31 December 2006, reaching US\$62 billion. Net new money inflows during the six months to 30 June 2007 were US\$5 billion, with strong client appetite for investment funds and discretionary products. The value of funds invested in HSBC's Investment Solutions suite of discretionary managed products reached US\$2.1 billion, a 47 per cent increase since 31 December 2006.

Operating expenses for the six months to 30 June 2007 were US\$109 million, 27 per cent higher than in the first half of 2006. This was mainly due to the recruitment of new, largely front-office, staff to support increased levels of activity. Performance-related remuneration rose as a consequence of higher revenue.

**Other** was lower due to the non-recurrence of two large gains reported in the first half of 2006: US\$101 million arising on the sale of part of HSBC's stake in UTI Bank Limited, an Indian retail bank, and US\$100 million from the disposal of Hang Seng Bank Limited's head office building.



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HSBC HOLDINGS PLC

**Business Review** (continued)

Profit/(loss) before tax and balance sheet data by customer group and global business

Half-year to 30 June 2007

| Hong Kong   | Personal<br>Financial<br>Services<br>US\$m | Commercial<br>Banking<br>US\$m | Corporate,<br>Investment<br>Banking &<br>Markets<br>US\$m | Private<br>Banking<br>US\$m | Other<br>US\$m | Inter-<br>segment<br>elimination<br>US\$m | Total<br>US\$m |
|---|--|--------------------------------|---|-----------------------------|----------------|---|----------------|
| Net interest income/(expense)   | 1,588                                      | 726                            | 418   | 49                          | (372)          | 159                                       | 2,568          |
| Net fee income  | 791  | 250                            | 318   | 80                          |                |   | 1,439          |
| Trading income/(expense)<br>excluding net interest income   | 74   | 32                             | 302   | 130                         | (13)           |   | 525            |
| Net interest income on trading<br>activities  | 2  |                                | 80  |                             | 21             | (159)                                     | (56)           |
| Net trading income  | 76   | 32                             | 382   | 130                         | 8              | (159)                                     | 469            |
| Net income/(expense) from<br>financial instruments designated at<br>fair value                      | 273  | (36)                           | 1   |                             | (28)           |   | 210            |
| Gains less losses from financial<br>investments   |  |                                | 1   | 1                           | 30             |   | 32             |
| Dividend income   | 1  |                                | 1   |                             | 15             |   | 17             |
| Net earned insurance premiums   | 1,366                                      | 55                             | 5   |                             |                |   | 1,426          |
| Other operating income  | 97   | 13                             | 55  | 10                          | 390            | (152)                                     | 413            |
| <b>Total operating income</b>   | <b>4,192</b>                               | <b>1,040</b>                   | <b>1,181</b>  | <b>270</b>                  | <b>43</b>      | <b>(152)</b>                              | <b>6,574</b>   |
| Net insurance claims <sup>1</sup>   | (1,473)                                    | (34)                           | (5)   |                             |                |   | (1,512)        |
| <b>Net operating income before<br/>loan impairment charges and<br/>other credit risk provisions</b> | <b>2,719</b>                               | <b>1,006</b>                   | <b>1,176</b>  | <b>270</b>                  | <b>43</b>      | <b>(152)</b>                              | <b>5,062</b>   |
| Loan impairment charges and<br>other credit risk provisions   | (74)                                       | (1)                            | (5)   |                             |                |   | (80)           |
| <b>Net operating income</b>   | <b>2,645</b>                               | <b>1,005</b>                   | <b>1,171</b>  | <b>270</b>                  | <b>43</b>      | <b>(152)</b>                              | <b>4,982</b>   |
| Total operating expenses  | (750)                                      | (246)                          | (474)   | (109)                       | (238)          | 152                                       | (1,665)        |
| <b>Operating profit/(loss)</b>  | <b>1,895</b>                               | <b>759</b>                     | <b>697</b>  | <b>161</b>                  | <b>(195)</b>   |   | <b>3,317</b>   |
| Share of profit in associates and<br>joint ventures   | 3  | 1                              |   |                             | 9              |   | 13             |
| <b>Profit/(loss) before tax</b>   | <b>1,898</b>                               | <b>760</b>                     | <b>697</b>  | <b>161</b>                  | <b>(186)</b>   |   | <b>3,330</b>   |

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|                                   | %    | %    | %    | %    | %     | %    |
|-----------------------------------|------|------|------|------|-------|------|
| Share of HSBC's profit before tax | 13.4 | 5.4  | 4.9  | 1.1  | (1.3) | 23.5 |
| Cost efficiency ratio             | 27.6 | 24.5 | 40.3 | 40.4 | 553.5 | 32.9 |

**Balance sheet data<sup>2</sup>**

|  | US\$m   | US\$m  | US\$m   | US\$m  | US\$m  | US\$m   |
|--|---------|--------|---------|--------|--------|---------|
| Loans and advances to customers (net)  | 39,375  | 25,105 | 19,231  | 4,309  | 1,898  | 89,918  |
| Total assets   | 62,199  | 31,043 | 163,766 | 12,553 | 31,120 | 300,681 |
| Customer accounts  | 120,638 | 44,719 | 26,978  | 12,340 | 544    | 205,219 |
| Loans and advances to banks (net) <sup>3</sup>   |         |        | 61,850  |        |        |         |
| Trading assets, financial instruments designated at fair value, and financial investments <sup>3</sup> |         |        | 72,996  |        |        |         |
| Deposits by banks <sup>3</sup>   |         |        | 9,991   |        |        |         |

For footnotes, see page 40.

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Half-year to 30 June 2006

| <b>Hong Kong</b>  | Personal<br>Financial<br>Services<br>US\$m | Commercial<br>Banking<br>US\$m | Corporate,<br>Investment<br>Banking &<br>Markets<br>US\$m | Private<br>Banking<br>US\$m | Other<br>US\$m | Inter-<br>segment<br>elimination<br>US\$m | Total<br>US\$m |
|---|--|--------------------------------|---|-----------------------------|----------------|---|----------------|
| Net interest income/(expense)   | 1,383                                      | 622                            | 213   | 34                          | (312)          | 218                                       | 2,158          |
| Net fee income/(expense)  | 477  | 219                            | 282   | 58                          | (36)           |   | 1,000          |
| Trading income/(expense)<br>excluding net interest income   | 44   | 27                             | 333   | 105                         | (55)           |   | 454            |
| Net interest income on trading<br>activities  | 2  |                                | 19  |                             | 49             | (218)                                     | (148)          |
| Net trading income/(expense)  | 46   | 27                             | 352   | 105                         | (6)            | (218)                                     | 306            |
| Net income/(expense) from<br>financial instruments designated<br>at fair value                      | 17   | (41)                           | 2   |                             | 28             |   | 6              |
| Gains less losses from financial<br>investments   | 11   |                                | (1)   | 6                           | 106            |   | 122            |
| Dividend income   |  |                                | 1   |                             | 58             |   | 59             |
| Net earned insurance premiums   | 1,265                                      | 44                             | 8   |                             |                |   | 1,317          |
| Other operating income  | 104  | 9                              | 32  | 5                           | 425            | (132)                                     | 443            |
| <b>Total operating income</b>   | <b>3,303</b>                               | <b>880</b>                     | <b>889</b>  | <b>208</b>                  | <b>263</b>     | <b>(132)</b>                              | <b>5,411</b>   |
| Net insurance claims <sup>1</sup>   | (1,164)                                    | (23)                           | (6)   |                             |                |   | (1,193)        |
| <b>Net operating income before loan<br/>impairment charges and other<br/>credit risk provisions</b> | <b>2,139</b>                               | <b>857</b>                     | <b>883</b>  | <b>208</b>                  | <b>263</b>     | <b>(132)</b>                              | <b>4,218</b>   |
| Loan impairment (charges)/<br>recoveries and other credit risk<br>provisions                        | (55)                                       | (38)                           | 23  |                             |                |   | (70)           |
| <b>Net operating income</b>   | <b>2,084</b>                               | <b>819</b>                     | <b>906</b>  | <b>208</b>                  | <b>263</b>     | <b>(132)</b>                              | <b>4,148</b>   |
| <b>Total operating expenses</b>   | <b>(666)</b>                               | <b>(232)</b>                   | <b>(429)</b>  | <b>(85)</b>                 | <b>(224)</b>   | <b>132</b>                                | <b>(1,504)</b> |
| <b>Operating profit</b>   | <b>1,418</b>                               | <b>587</b>                     | <b>477</b>  | <b>123</b>                  | <b>39</b>      |   | <b>2,644</b>   |
| Share of profit in associates and<br>joint ventures   | 2  |                                |   |                             | 8              |   | 10             |
| <b>Profit before tax</b>  | <b>1,420</b>                               | <b>587</b>                     | <b>477</b>  | <b>123</b>                  | <b>47</b>      |   | <b>2,654</b>   |
|   | %  | %                              | %   | %                           | %              |   | %              |
| Share of HSBC's profit before tax   | 11.3                                       | 4.7                            | 3.8   | 1.0                         | 0.4            |   | 21.2           |
| Cost efficiency ratio   | 31.1                                       | 27.1                           | 48.6  | 40.9                        | 85.2           |   | 35.7           |
| <b>Balance sheet data<sup>2</sup></b>   | <b>US\$m</b>                               | <b>US\$m</b>                   | <b>US\$m</b>  | <b>US\$m</b>                | <b>US\$m</b>   |   | <b>US\$m</b>   |
| Loans and advances to customers<br>(net)  | 34,944                                     | 21,932                         | 23,997  | 3,376                       | 1,905          |   | 86,154         |

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|  |         |        |         |        |        |         |
|--|---------|--------|---------|--------|--------|---------|
| Total assets   | 55,544  | 27,626 | 135,938 | 9,694  | 17,979 | 246,781 |
| Customer accounts  | 110,536 | 36,234 | 22,550  | 10,502 | 345    | 180,167 |
| Loans and advances to banks<br>(net) <sup>3</sup>  |         |        | 40,230  |        |        |         |
| Trading assets, financial<br>instruments designated at fair<br>value, and financial investments <sup>3</sup> |         |        | 62,845  |        |        |         |
| Deposits by banks <sup>3</sup>   |         |        | 5,379   |        |        |         |

For footnotes, see page 40.



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HSBC HOLDINGS PLC

**Business Review** (continued)

Profit/(loss) before tax and balance sheet data by customer group and global business (continued)

Half-year to 31 December 2006

|   | Personal<br>Financial<br>Services<br>US\$m | Commercial<br>Banking<br>US\$m | Corporate<br>Investment,<br>Banking &<br>Markets<br>US\$m | Private<br>Banking<br>US\$m | Other<br>US\$m | Inter-<br>segment<br>elimination<br>US\$m | Total<br>US\$m |
|---|--|--------------------------------|---|-----------------------------|----------------|---|----------------|
| <b>Hong Kong</b>  |  |                                |   |                             |                |   |                |
| Net interest income/(expense)   | 1,499                                      | 722                            | 340   | 42                          | (334)          | 258                                       | 2,527          |
| Net fee income  | 500  | 235                            | 252   | 65                          | 4              |   | 1,056          |
| Trading income excluding net interest income  | 40   | 30                             | 240   | 71                          | 89             |   | 470            |
| Net interest income on trading activities   | 2  |                                | 69  |                             | 28             | (258)                                     | (159)          |
| Net trading income  | 42   | 30                             | 309   | 71                          | 117            | (258)                                     | 311            |
| Net income/(expense) from financial instruments designated at fair value                    | 356  | (12)                           | 3   | 1                           | (94)           |   | 254            |
| Gains less losses from financial investments  | 3  |                                |   | 3                           | 34             |   | 40             |
| Dividend income   | 1  | 1                              | 1   |                             | (1)            |   | 2              |
| Net earned insurance premiums   | 1,254                                      | 51                             | 6   |                             |                |   | 1,311          |
| Other operating income  | 98   | 24                             | 49  | 8                           | 356            | (144)                                     | 391            |
| <b>Total operating income</b>   | <b>3,753</b>                               | <b>1,051</b>                   | <b>960</b>  | <b>190</b>                  | <b>82</b>      | <b>(144)</b>                              | <b>5,892</b>   |
| Net insurance claims <sup>1</sup>   | (1,474)                                    | (27)                           | (5)   |                             |                |   | (1,506)        |
| <b>Net operating income before loan impairment charges and other credit risk provisions</b> | <b>2,279</b>                               | <b>1,024</b>                   | <b>955</b>  | <b>190</b>                  | <b>82</b>      | <b>(144)</b>                              | <b>4,386</b>   |
| Loan impairment (charges)/ recoveries and other credit risk provisions                      | (64)                                       | (31)                           | 4   |                             | (11)           |   | (102)          |
| <b>Net operating income</b>   | <b>2,215</b>                               | <b>993</b>                     | <b>959</b>  | <b>190</b>                  | <b>71</b>      | <b>(144)</b>                              | <b>4,284</b>   |
| <b>Total operating expenses</b>   | <b>(756)</b>                               | <b>(259)</b>                   | <b>(482)</b>  | <b>(112)</b>                | <b>(300)</b>   | <b>144</b>                                | <b>(1,765)</b> |
| <b>Operating profit/(loss)</b>  | <b>1,459</b>                               | <b>734</b>                     | <b>477</b>  | <b>78</b>                   | <b>(229)</b>   |   | <b>2,519</b>   |
| Share of profit in associates and joint ventures  | 1  |                                | 1   |                             | 7              |   | 9              |

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|  |         |        |         |        |        |         |
|--|---------|--------|---------|--------|--------|---------|
| Profit/(loss) before tax   | 1,460   | 734    | 478     | 78     | (222)  | 2,528   |
|  | %       | %      | %       | %      | %      | %       |
| Share of HSBC's profit before tax  | 15.3    | 7.7    | 4.9     | 0.8    | (2.3)  | 26.4    |
| Cost efficiency ratio  | 33.2    | 25.3   | 50.5    | 58.9   | 365.9  | 40.2    |
| Balance sheet data <sup>2</sup>  |         |        |         |        |        |         |
|  | US\$m   | US\$m  | US\$m   | US\$m  | US\$m  | US\$m   |
| Loans and advances to customers (net)  | 35,445  | 23,520 | 20,270  | 3,081  | 1,966  | 84,282  |
| Total assets   | 57,348  | 29,786 | 153,200 | 10,462 | 21,632 | 272,428 |
| Customer accounts  | 118,201 | 41,493 | 24,530  | 11,991 | 476    | 196,691 |
| Loans and advances to banks (net) <sup>3</sup>   |         |        | 45,023  |        |        |         |
| Trading assets, financial instruments designated at fair value, and financial investments <sup>3</sup> |         |        | 80,036  |        |        |         |
| Deposits by banks <sup>3</sup>   |         |        | 4,363   |        |        |         |

1 Net insurance claims incurred and movement in policyholders' liabilities.

2 Third party only.

3 These assets and liabilities were significant to Corporate, Investment Banking and Markets.

[Back to Contents](#)**Rest of Asia-Pacific (including the Middle East)**

Profit/(loss) before tax by country within customer groups and global businesses

|                                      | Personal<br>Financial<br>Services<br>US\$m | Commercial<br>Banking<br>US\$m | Corporate,<br>Investment<br>Banking &<br>Markets<br>US\$m | Private<br>Banking<br>US\$m | Other<br>US\$m | Total<br>US\$m |
|--------------------------------------|--|--------------------------------|---|-----------------------------|----------------|----------------|
| <b>Half-year to 30 June 2007</b>     |  |                                |   |                             |                |                |
| Australia                            | 19   | 16                             | 16  |                             |                | 51             |
| India                                | (13)                                       | 49                             | 211   |                             | 52             | 299            |
| Indonesia                            | 2  | 15                             | 46  |                             | (5)            | 58             |
| Japan                                | (8)  | (1)                            | 26  | 1                           |                | 18             |
| Mainland China                       | 168  | 171                            | 126   |                             | 1,084          | 1,549          |
| Malaysia                             | 40   | 28                             | 70  | 1                           | 6              | 145            |
| Middle East                          | 125  | 220                            | 216   | 1                           | 44             | 606            |
| Egypt                                | 7  | 22                             | 24  |                             | 19             | 72             |
| United Arab Emirates                 | 62   | 139                            | 93  | 1                           |                | 295            |
| Other Middle East                    | 37   | 41                             | 53  |                             | (3)            | 128            |
| Middle East (excluding Saudi Arabia) | 106  | 202                            | 170   | 1                           | 16             | 495            |
| Saudi Arabia                         | 19   | 18                             | 46  |                             | 28             | 111            |
| Singapore                            | 50   | 60                             | 105   | 51                          | 1              | 267            |
| South Korea                          | (15)                                       | (8)                            | 66  |                             | 15             | 58             |
| Taiwan                               | (35)                                       | 13                             | 64  |                             | 1              | 43             |
| Other                                | 18   | 34                             | 152   | 2                           | 44             | 250            |
|                                      | <b>351</b>                                 | <b>597</b>                     | <b>1,098</b>  | <b>56</b>                   | <b>1,242</b>   | <b>3,344</b>   |
| <b>Half-year to 30 June 2006</b>     |  |                                |   |                             |                |                |
| Australia                            | 12   | 17                             | 20  |                             |                | 49             |
| India                                |  | 22                             | 143   | 1                           | 49             | 215            |
| Indonesia                            | (12)                                       | 16                             | 35  |                             | (12)           | 27             |
| Japan                                |  | (2)                            | 28  | (1)                         |                | 25             |
| Mainland China                       | 94   | 106                            | 73  |                             | 7              | 280            |
| Malaysia                             | 37   | 42                             | 49  | (1)                         | 1              | 128            |
| Middle East                          | 160  | 185                            | 201   | 1                           | 12             | 559            |
| Egypt                                | 5  | 20                             | 17  |                             | 9              | 51             |
| United Arab Emirates                 | 38   | 105                            | 60  |                             |                | 203            |
| Other Middle East                    | 39   | 41                             | 44  | 1                           | (1)            | 124            |
| Middle East (excluding Saudi Arabia) | 82   | 166                            | 121   | 1                           | 8              | 378            |
| Saudi Arabia                         | 78   | 19                             | 80  |                             | 4              | 181            |
| Singapore                            | 35   | 42                             | 72  | 42                          | (6)            | 185            |
| South Korea                          | (15)                                       | (8)                            | 63  |                             | 8              | 48             |
| Taiwan                               | (117)                                      | 14                             | 60  |                             |                | (43)           |
| Other                                | 11   | 64                             | 95  | 6                           | 8              | 184            |

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|                                      | 205  | 498  | 839 | 48 | 67   | 1,657 |
|--------------------------------------|------|------|-----|----|------|-------|
| Half-year to 31 December 2006        |      |      |     |    |      |       |
| Australia                            | 64   | 15   | 26  |    |      | 105   |
| India                                | (24) | 24   | 134 | 1  | 43   | 178   |
| Indonesia                            | (10) | 30   | 34  |    | (10) | 44    |
| Japan                                | (3)  |      | 21  |    | 80   | 98    |
| Mainland China                       | 182  | 135  | 94  |    | 17   | 428   |
| Malaysia                             | 40   | 45   | 50  |    | 11   | 146   |
| Middle East                          | 75   | 171  | 195 | 1  | 34   | 476   |
| Egypt                                | 4    | 21   | 18  |    | 11   | 54    |
| United Arab Emirates                 | 30   | 97   | 78  |    | (2)  | 203   |
| Other Middle East                    | 22   | 33   | 39  | 1  |      | 95    |
| Middle East (excluding Saudi Arabia) | 56   | 151  | 135 | 1  | 9    | 352   |
| Saudi Arabia                         | 19   | 20   | 60  |    | 25   | 124   |
| Singapore                            | 38   | 48   | 73  | 26 | (5)  | 180   |
| South Korea                          | (40) | (12) | 52  |    | 11   | 11    |
| Taiwan                               | (62) | 23   | 58  |    | 1    | 20    |
| Other                                | 12   | 57   | 73  | 4  | 38   | 184   |
|                                      | 272  | 536  | 810 | 32 | 220  | 1,870 |

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HSBC HOLDINGS PLC

**Business Review** (continued)

## Loans and advances to customers (net) by country

|                                      | Half-year to  |               |               |
|--------------------------------------|---------------|---------------|---------------|
|                                      | 30 June       | 30 June       | 31            |
|                                      | 2007          | 2006          | December      |
|                                      | US\$m         | US\$m         | US\$m         |
| Australia                            | 9,845         | 9,824         | 8,775         |
| India                                | 6,216         | 4,139         | 4,915         |
| Indonesia                            | 1,296         | 1,297         | 1,337         |
| Japan                                | 3,580         | 3,581         | 3,391         |
| Mainland China                       | 6,787         | 5,477         | 6,065         |
| Malaysia                             | 8,003         | 7,150         | 7,747         |
| Middle East (excluding Saudi Arabia) | 17,047        | 14,553        | 15,622        |
| Egypt                                | 1,196         | 963           | 965           |
| United Arab Emirates                 | 10,928        | 9,433         | 10,122        |
| Other Middle East                    | 4,923         | 4,157         | 4,535         |
| Singapore                            | 10,768        | 10,108        | 9,610         |
| South Korea                          | 6,458         | 5,623         | 6,260         |
| Taiwan                               | 3,834         | 3,977         | 3,974         |
| Other                                | 14,340        | 9,110         | 9,878         |
|                                      | <b>88,174</b> | <b>74,839</b> | <b>77,574</b> |

## Customer accounts by country

|                                      | Half-year to |         |          |
|--------------------------------------|--------------|---------|----------|
|                                      | 30 June      | 30 June | 31       |
|                                      | 2007         | 2006    | December |
|                                      | US\$m        | US\$m   | US\$m    |
| Australia                            | 10,345       | 7,652   | 8,491    |
| India                                | 8,827        | 5,861   | 7,936    |
| Indonesia                            | 2,082        | 2,090   | 2,082    |
| Japan                                | 3,944        | 6,069   | 4,186    |
| Mainland China                       | 9,229        | 5,825   | 6,941    |
| Malaysia                             | 10,629       | 8,500   | 9,640    |
| Middle East (excluding Saudi Arabia) | 26,277       | 17,517  | 21,196   |
| Egypt                                | 3,358        | 2,318   | 2,703    |
| United Arab Emirates                 | 15,362       | 9,200   | 11,166   |

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|                   |                |        |         |
|-------------------|----------------|--------|---------|
| Other Middle East | <b>7,557</b>   | 5,999  | 7,327   |
| Singapore         | <b>25,885</b>  | 21,007 | 23,517  |
| South Korea       | <b>4,705</b>   | 3,297  | 3,890   |
| Taiwan            | <b>9,208</b>   | 7,522  | 7,675   |
| Other             | <b>16,328</b>  | 11,919 | 13,441  |
|                   | <b>127,459</b> | 97,259 | 108,995 |

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Profit before tax

|   | Half-year<br>to          |                          |                                 |
|---|--------------------------|--------------------------|---------------------------------|
|   | 30 June<br>2007<br>US\$m | 30 June<br>2006<br>US\$m | 31<br>December<br>2006<br>US\$m |
| <b>Rest of Asia-Pacific (including the Middle East)</b>                                     |                          |                          |                                 |
| Net interest income   | 1,901                    | 1,479                    | 1,568                           |
| Net fee income  | 1,010                    | 785                      | 837                             |
| Net trading income  | 797                      | 551                      | 630                             |
| Net income/(expense) from financial instruments designated at fair value                    | 78                       | (5)                      | 84                              |
| Gains less losses from financial investments  | 26                       | 27                       | 14                              |
| Gains arising from dilution of interests in associates                                      | 1,076                    |                          |                                 |
| Dividend income   | 4                        |                          | 5                               |
| Net earned insurance premiums   | 109                      | 89                       | 85                              |
| Other operating income  | 360                      | 288                      | 477                             |
| <b>Total operating income</b>   | <b>5,361</b>             | <b>3,214</b>             | <b>3,700</b>                    |
| Net insurance claims incurred and movement in policyholders' liabilities                    | (141)                    | (63)                     | (129)                           |
| <b>Net operating income before loan impairment charges and other credit risk provisions</b> | <b>5,220</b>             | <b>3,151</b>             | <b>3,571</b>                    |
| Loan impairment charges and other credit risk provisions                                    | (308)                    | (271)                    | (241)                           |
| <b>Net operating income</b>   | <b>4,912</b>             | <b>2,880</b>             | <b>3,330</b>                    |
| Total operating expenses  | (2,075)                  | (1,609)                  | (1,939)                         |
| <b>Operating profit</b>   | <b>2,837</b>             | <b>1,271</b>             | <b>1,391</b>                    |
| Share of profit in associates and joint ventures  | 507                      | 386                      | 479                             |
| <b>Profit before tax</b>  | <b>3,344</b>             | <b>1,657</b>             | <b>1,870</b>                    |
|   | %                        | %                        | %                               |
| Share of HSBC's profit before tax   | 23.6                     | 13.2                     | 19.5                            |
| Cost efficiency ratio   | 39.8                     | 51.1                     | 54.3                            |
| Period-end staff numbers (full-time equivalent)   | 81,031                   | 63,299                   | 72,265                          |

Balance sheet data<sup>1</sup>

|   | US\$m   | US\$m   | US\$m   |
|---|---------|---------|---------|
| Loans and advances to customers (net)   | 88,174  | 74,839  | 77,574  |
| Loans and advances to banks (net)   | 34,678  | 26,459  | 27,517  |
| Trading assets, financial instruments designated at fair value, and financial investments | 52,189  | 38,538  | 41,585  |
| Total assets  | 201,123 | 168,857 | 167,668 |
| Deposits by banks   | 13,709  | 9,179   | 10,323  |
| Customer accounts   | 127,459 | 97,259  | 108,995 |

<sup>1</sup> Third party only.

Economic briefing

**Mainland China** s economy continued to expand strongly, as GDP growth accelerated to 11.5 per cent in the first half of 2007 as urban fixed-asset investment also rose. Higher incomes triggered the fastest growth in retail sales for 10 years. Despite a slowdown in US GDP growth, Chinese exports remained strong. Concerns about CPI inflation emerged as it exceeded 3 per cent year-on-year in March, but much of this was due to supply shocks in the food sector, notably the effect on food prices of a disease among pigs. These events prompted fresh measures to tighten the economy, though they were

moderate and the authorities demonstrated no desire to slow growth too sharply. As a result, bank credit and broad money supply in June grew by more than 16 per cent and 17 per cent, respectively, year-on-year. The government also moved to gently deflate the stock market by raising transaction taxes. The renminbi continued its gradual appreciation against the US dollar.

**Japan** s economy, which remains the largest in the region, continued to expand in the first half of 2007. Exports rose steadily, while growth of private capital investment remained firm and consumer spending rebounded. Core consumer prices fell,



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## Business Review (continued)

however, making it difficult for the Bank of Japan to raise interest rates. Corporate sector borrowing continued to recover, although at a modest pace.

The economies of the **Middle East** continued to perform well in the first half of 2007. Although headline growth rates were less than those seen in the past four years, as oil prices moderated and OPEC-mandated production cuts started to take effect, underlying performance remained very strong. Household and government consumption continued their recent upward trend as oil revenues fed into the domestic economies, supported by low real interest rates and significant population growth. Investment spending was also strong, focusing on infrastructure projects sponsored and, in some cases, financed by government. Public finances, trade and current account positions all remained robust. Domestic demand, high liquidity and the weakness of the US dollar boosted inflationary pressures although, generally, price rises remained at around 5 per cent. The region's equity markets began to bounce back from the lows of 2005 and 2006, with the exception of Saudi Arabia, which was subdued.

**Elsewhere in Asia**, most economies continued to perform impressively in the first half of 2007, particularly India, Vietnam, Indonesia, the Philippines and Singapore. Export growth slowed moderately, partly due to inventory adjustment in technology sectors, although domestic consumption and investment demand generally improved, the latter in response to high capacity utilisation, low interest rates and quickening credit growth. Despite strong domestic growth and continued firmness in commodity prices, there was a general, and substantial, reduction in inflation as the effect of previous oil price rises dropped out and many currencies strengthened against the US dollar. In Indonesia and Thailand, monetary policy was eased, while in most other countries it was kept largely unchanged. The main exception was India, where consumer price inflation accelerated considerably and the Reserve Bank of India is expected to tighten monetary policy. Asian currencies were generally mixed against the US dollar in the first half of 2007, though the Indian rupee, Indonesian rupiah, Malaysian ringgit, Philippine peso and Thai baht all strengthened.

### Review of business performance

HSBC's operations in the Rest of Asia-Pacific region reported a pre-tax profit of US\$3,344 million compared with US\$1,657 million in the first half of 2006, an increase of 102 per cent. On an underlying basis, pre-tax profits grew by 96 per cent. During the period, exceptional profits of US\$1,076 million were

recognised in the Other segment following share offerings by HSBC's associates, Ping An Insurance, Bank of Communications and Industrial Bank. Excluding these dilution gains and on an underlying basis, profit before tax increased by 33 per cent.

HSBC's focus on emerging markets supported continued growth in the region, with underlying net operating income (excluding dilution gains) increasing by 29 per cent, driven by strong performances in mainland China, India, the Middle East and Singapore.

CIBM's increased profit before tax, largely from the success of coordinated global service product offerings. The rise in Commercial Banking revenues was driven by active customer acquisition and balance sheet growth. In Personal Financial Services, profit before tax increased as a result of balance sheet growth and higher fee income. Loan impairment charges decreased and credit conditions remained benign. Private Banking delivered solid progress in light of growing wealth in the region.

The following commentary is on an underlying basis.

**Personal Financial Services** reported a pre-tax profit of US\$351 million, an increase of 62 per cent compared with the first half of 2006. Net operating income increased due to balance sheet growth and higher fee income. Loan impairment charges declined by 14 per cent and credit conditions remained benign. Continued investment in new branches and the expansion of operations caused the cost efficiency ratio to rise slightly to 68.9 per cent.

Across the region, HSBC achieved significant profit before tax growth, with six countries reporting increases of over 30 per cent. Overall, HSBC attracted 800,000 more customers than at 30 June 2006, more than half of which were located in India.

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In mainland China, pre-tax profit grew by 73 per cent as a result of strong performances from associates and notable deposit growth following a 36 per cent increase in the number of customers in the operating business.

In Singapore, pre-tax profit increased by 35 per cent, as insurance increased its contribution to the business and asset spreads improved.

In the Middle East outside Saudi Arabia, pre-tax profit increased by 32 per cent. Volume-driven growth in net interest income and fees, particularly in the United Arab Emirates, drove improved performance. There was a reduced contribution from HSBC's associate, The Saudi British Bank, as a

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result of lower stock market activity following a correction to the market in 2006.

Net interest income rose by 22 per cent, due to higher asset and deposit balances. Average deposit balances increased by 32 per cent as the Group focused on growing the mass-affluent Premier customer base. India, Singapore, and the Middle East experienced the strongest deposit growth. Other deposit initiatives included HSBC Direct in Taiwan and South Korea, which generated 120,000 new accounts, with total savings balances exceeding US\$900 million, and renminbi-denominated services designed to attract new Premier clients in eight priority cities in mainland China.

Average asset balances increased and spreads widened. Average loans and advances to customers rose by 42 per cent, as both credit card and personal lending grew. Growth in the latter was particularly robust in India following the expansion of the branch network there and greater marketing activity.

Cards in circulation rose to 8.3 million and card balances were 23 per cent higher than at 30 June 2006. HSBC continued to benefit from increased cardholder spending, which grew by 32 per cent. In the Middle East, credit card balances rose by 47 per cent, due in part to a successful promotional initiative.

Average mortgage balances remained broadly in line with the first half of 2006, notwithstanding the sale of a mortgage portfolio in Australia in the second half of 2006. Excluding that transaction, growth was 7 per cent as a result of demand across the region.

Net fee income rose by 25 per cent to US\$336 million, with continued strong growth in the cards and wealth management businesses. Compared with the first half of 2006, HSBC increased the number of customers in its key Premier segment by 32 per cent.

Sales of investment products across the region increased by 23 per cent. Particularly strong sales were recorded in the Middle East, South Korea, Malaysia and Singapore. In mainland China, HSBC was among the first to launch an expanded Qualified Domestic Institutional Investor offering, providing residents with a new renminbi-denominated product. Overall, funds under management in the region grew by 12 per cent to US\$10.3 billion.

Insurance premiums increased due to consumer demand and the expansion of HSBC's distribution capabilities. This was partially offset by higher net claims. In Malaysia, HSBC Amanah Takaful

launched the first *shariah*-compliant investment-linked structured product.

Loan impairment charges and other credit risk provisions fell by 14 per cent. In Indonesia, higher recoveries resulted from improved collection efforts and, in Taiwan, lower impairment charges were recorded, mainly due to the government debt negotiation mechanism that led to a deterioration in the credit environment and higher impairment charges in the first half of 2006. This was partially offset by higher charges for cards in India, Malaysia and Thailand.

Additional investment in building distribution platforms led to a 24 per cent rise in operating expenses to US\$911 million, with the Middle East, India, South Korea and Indonesia experiencing the most substantial increases. In the Middle East, client-facing staff were hired to augment sales of loans, cards and mortgages, and IT expenditure on new internet banking and credit card infrastructure rose. In India and Indonesia, card and consumer finance-related investment costs were incurred to expand these businesses. In South Korea, increased staff and infrastructure expenditure was related to the implementation of HSBC Direct.

Income from HSBC's investments in associates increased by 9 per cent, due to the strong performance of Ping An Insurance. In the Middle East, The Saudi British Bank's performance decreased compared with the first half of 2006, due to the ongoing effects of a correction in the local stock market in the middle of 2006.

**Commercial Banking** reported a record profit before tax of US\$597 million, 17 per cent higher than in the first half of 2006. The dynamic performance of the region's economies supported active customer acquisition and strong balance sheet growth. Several major areas in the region reported increases in profit before tax in excess of 30 per cent, with outstanding performances in India, Singapore, mainland China and the United Arab Emirates. Notwithstanding expansion of these businesses through investments in staff, infrastructure and new products, the cost efficiency ratio improved by 1.8 percentage points.

HSBC's Middle East operations continued to benefit from strong economic growth. Profit before tax grew by 18 per cent as a result of improved balance sheet utilisation, supported by a benign credit environment and greater transaction banking revenues. Profit before tax rose by 12 per cent in Egypt compared with the first half of 2006, but strong revenue growth was masked by fewer loan impairment releases.



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## Business Review (continued)

In India and Singapore, profit before tax grew by 110 per cent and 35 per cent respectively, as net interest income benefited from higher deposit balances.

The local incorporation of HSBC's business in mainland China added impetus to its operations by permitting the scope of services to be expanded, contributing to growth in profit before tax of 55 per cent.

In Australia, total revenues grew by 16 per cent due to new client acquisitions. Profit before tax growth was lower, however, due to the non-recurrence of impairment releases in 2006.

HSBC continued to develop its cross-border capabilities and initiatives for small businesses, rolling out small-business banking in Bahrain, Qatar and Jordan. An additional six International Banking Centres were opened in the Middle East and one in Mauritius, bringing the total in the Rest of Asia-Pacific region to 16. Country desks were established by HSBC in mainland China to facilitate cross-border transactions with South Korea and Taiwan.

Global relationship management capabilities were improved with the release of a centralised cross-border client relationship management database in ten countries. New relationship managers were recruited to the Dubai business banking unit for small business customers, increasing revenues by 39 per cent. The small and micro business customer base expanded with the implementation of a loyalty campaign, enhanced internet banking capabilities and the acquisition of Chailease Credit Services, a factoring company in Taiwan, to facilitate cross-border transactions.

Net interest income grew by 26 per cent to US\$517 million, with the opening of 7 new branches in the region delivering deposit and loan growth. Campaigns targeted at growing deposit balances were initiated and growth in average deposits was 43 per cent. Interest rate rises contributed to higher deposit spreads.

In India, a strategic expansion into provincial cities helped trigger strong deposit and lending growth which combined with widening asset spreads to increase small and medium business income by 46 per cent.

In the Middle East, HSBC generated higher net interest income from increases in both liabilities and lending, particularly in the United Arab Emirates. Balances rose as regional liquidity growth underpinned an increase in domestic purchasing power in Middle Eastern countries. The resultant rise

in demand for goods and services stimulated trade in the region.

In mainland China, marketing campaigns stimulated strong growth in both assets and liabilities. Net interest income also benefited from a significant increase in liability spreads, and a campaign for deposit accounts led customers to open new foreign currency accounts.

Lending balances in Malaysia grew after successful campaigns focused on identifying and following up on new business. The cross-border referral system used by HSBC, Global Links, and regional alignments were instrumental in growing successful referrals by 75 per cent. Campaigns targeted at increasing liability balances were launched in Taiwan and Australia.

Net fee income increased by 22 per cent, driven by higher trade services income and guarantee fees in the Middle East, and growth in credit and custody fees in India. HSBC introduced a number of initiatives to support small and medium business trade, including TradeSmart in Malaysia and Tradeline in Bangladesh. HSBC continued to invest in direct channel capabilities, and customers initiated more transactions using business internet banking.

Trading income increased by 32 per cent as a result of the recently launched online e-trading platform, which drove additional volume, and increased customer demand for hedging products in India and Singapore.

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Revenues from insurance products in Singapore grew by 112 per cent as a result of increased general insurance business and higher investment income.

Loan impairment charges of US\$54 million compared with net releases in 2006, largely due to higher loan volumes and fewer releases of allowances, particularly in Australia and Malaysia. Higher loan volumes and downgrades of a few customers in Sri Lanka, Thailand and Malaysia increased loan impairment charges but these were partly offset by recoveries on specific accounts in Singapore and Mauritius and reduced loan impairment charges in the Middle East, primarily due to the release of collective impairments. In the first half of 2006, there was a modest net recovery of loan impairment charges.

Total operating expenses grew by 20 per cent, driven by additional staff costs and performance-related expenses in India, the Middle East and mainland China. Higher costs in the region largely reflected increased sales and support staff for business initiatives and expansion. IT and marketing expenses were incurred in expanding direct banking

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capabilities in South Korea and adding new branches in India, mainland China and Malaysia. A dedicated Commercial Banking call centre was opened in the Philippines.

Income from associates increased by 43 per cent, as Ping An Insurance, Bank of Communications and Industrial Bank in mainland China all generated higher income.

**Corporate, Investment Banking and Markets** in Rest of Asia-Pacific reported a pre-tax profit of US\$1,098 million, which represented 26 per cent of the global business's pre-tax profits, and a rise of 28 per cent compared with the first half of 2006. The strong performance was driven by the effective distribution of global products to HSBC's clients throughout the region. The cost efficiency ratio improved by 0.6 percentage points to 34.1 per cent.

In the Middle East, a 7 per cent rise in pre-tax profit reflected strong income streams across most major businesses. HSBC's operations in India reported a 40 per cent increase in pre-tax profits with significant growth in net interest income and trading revenues.

In mainland China, pre-tax profits grew by 65 per cent, driven by strong growth in deposits and higher income from securities services and payments and cash management activities.

In each of Singapore, Thailand and Malaysia, CIBM reported increases in pre-tax profits of more than 30 per cent, primarily due to improvements in balance sheet management revenues and strong trading and fee income.

Total operating income increased by 27 per cent to US\$1,494 million, against a backdrop of rapid growth in regional economies. Net interest income grew significantly, partly due to higher revenues in the payment and cash management business across most countries, with notable contributions from businesses in India, mainland China and Singapore. The benefit of higher deposit balances, driven by buoyant local economies, was enhanced by improved spreads following increases in interest rates. Balance sheet management also reported an increase, as funds from maturing assets were reinvested at higher yields.

Net fees increased by 25 per cent to US\$409 million. Higher revenues in securities services reflected increased client volumes, encouraged by continuing investor confidence in local stock markets. Assets under custody grew significantly, in part due to the acquisition of Westpac's sub-custody business in Australia and New Zealand in the second half of 2006.

The rise in net trading income was principally due to increased credit and rates and foreign exchange revenues across most countries, particularly in India, Indonesia, Malaysia and Thailand. Higher volumes were driven by increased volatility in foreign exchange and interest rates, as customer appetite for risk management products grew.

In the Middle East, the structured derivatives business gained momentum as demand for structured interest rate products from institutional and corporate customers continued. Underwriting and syndication fees were boosted by a number of high profile mandates, reflecting HSBC's strength in distribution and market-making activities.

Loan impairment charges were broadly in line with the comparable period in 2006.

Operating expenses increased by 25 per cent, partly due to higher performance-related incentives in response to robust growth in operating income. Higher volumes in the payments and cash management and securities services businesses led to increases in operating expenses. In Global Markets, support costs increased, particularly IT-related costs, reflecting initiatives to strengthen HSBC's operations in the region.

The share of profits in associates and joint ventures increased by 23 per cent reflecting higher contributions from HSBC's investments in Bank of Communication and Industrial Bank.

In the first half of the year, **Private Banking** delivered solid progress and, in light of growing wealth in the region, continued to invest in the expanding business. Pre-tax profits of US\$56 million were 17 per cent higher than in the first half of 2006. Growth in operating income was strong across the region, with the largest contribution from Singapore. In Japan and India, investment to expand HSBC's Private Banking operations continued. The cost efficiency ratio of 48.6 per cent was 3.4 percentage points better than at 30 June 2006.

Net interest income rose by 56 per cent to US\$28 million, driven primarily by enhanced treasury performance and higher lending to clients in Singapore.

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Fee income of US\$52 million was 33 per cent ahead of the first half of 2006. In Japan, strong sales of fund products following increased sales and marketing activity boosted fee income and, in Singapore, strong appetite among clients for exposure to strongly performing stock markets drove higher sales of structured products.



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HSBC HOLDINGS PLC

**Business Review** (continued)

Trading and other operating income decreased due to the effect of interest rate increases on money market spreads.

Client assets were 7 per cent greater than at 31 December 2006, with most of the increase invested in equities and funds.

Operating expenses were slightly higher than in the first half of 2006, as continued investment expenditure in building up onshore operations in Japan and India was partly offset by the release of deferred compensation expenses in Singapore.

**Other** recorded dilution gains of US\$1,076 million following share offerings made in Shanghai by HSBC's three associates: Ping An Insurance, Bank of Communications and Industrial

Bank, which all successfully raised new capital. The consequent dilution of HSBC's interests was considerably less than its share of the new monies raised, resulting in the gains recognised. For further details see Note 19 on the Financial Statements.

Activity in the Group Service Centres, primarily in India and China, continued to grow, reflecting expansion in the type and volume of tasks undertaken, supported by a 22 per cent increase in staff numbers to nearly 29,000. Costs rose by 32 per cent, substantially all of which were recharged to HSBC's customer groups and global businesses.

During the first half of 2007, three additional Group Service Centres became operational, with a further two under development.

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Profit before tax and balance sheet data by customer group and global business

Half-year to 30 June 2007

| Rest of Asia-Pacific (including the Middle East)  | Personal Financial Services | Commercial Banking | Corporate, Investment Banking & Markets | Private Banking | Other        | Inter-segment elimination | Total        |
|---|-----------------------------|--------------------|---|-----------------|--------------|---------------------------|--------------|
|   | US\$m                       | US\$m              | US\$m                                   | US\$m           | US\$m        | US\$m                     | US\$m        |
| Net interest income   | 914                         | 517                | 551                                     | 28              | 66           | (175)                     | 1,901        |
| Net fee income  | 336                         | 202                | 409                                     | 52              | 11           |                           | 1,010        |
| Trading income excluding net interest income  | 34                          | 58                 | 475                                     | 35              | 4            |                           | 606          |
| Net interest income/(expense) on trading activities   | (1)                         |                    | 14                                      |                 | 3            | 175                       | 191          |
| Net trading income  | 33                          | 58                 | 489                                     | 35              | 7            | 175                       | 797          |
| Net income from financial instruments designated at fair value                              | 55                          | 3                  | 5                                       |                 | 15           |                           | 78           |
| Gains less losses from financial investments  | 2                           | 4                  | 19                                      |                 | 1            |                           | 26           |
| Gains arising from dilution of interests in associates                                      |                             |                    |   |                 | 1,076        |                           | 1,076        |
| Dividend income   |                             |                    | 1                                       |                 | 3            |                           | 4            |
| Net earned insurance premiums   | 100                         | 9                  |   |                 |              |                           | 109          |
| Other operating income  | 20                          | 8                  | 20                                      | (6)             | 387          | (69)                      | 360          |
| <b>Total operating income</b>   | <b>1,460</b>                | <b>801</b>         | <b>1,494</b>                            | <b>109</b>      | <b>1,566</b> | <b>(69)</b>               | <b>5,361</b> |
| Net insurance claims <sup>1</sup>   | (137)                       | (4)                |   |                 |              |                           | (141)        |
| <b>Net operating income before loan impairment charges and other credit risk provisions</b> | <b>1,323</b>                | <b>797</b>         | <b>1,494</b>                            | <b>109</b>      | <b>1,566</b> | <b>(69)</b>               | <b>5,220</b> |
| Loan impairment charges and other credit risk provisions                                    | (252)                       | (54)               | (2)                                     |                 |              |                           | (308)        |
| <b>Net operating income</b>   | <b>1,071</b>                | <b>743</b>         | <b>1,492</b>                            | <b>109</b>      | <b>1,566</b> | <b>(69)</b>               | <b>4,912</b> |
| Total operating expenses  | (911)                       | (313)              | (510)                                   | (53)            | (357)        | 69                        | (2,075)      |
| <b>Operating profit</b>   | <b>160</b>                  | <b>430</b>         | <b>982</b>                              | <b>56</b>       | <b>1,209</b> |                           | <b>2,837</b> |
| Share of profit in associates and joint ventures  | 191                         | 167                | 116                                     |                 | 33           |                           | 507          |
| <b>Profit before tax</b>  | <b>351</b>                  | <b>597</b>         | <b>1,098</b>                            | <b>56</b>       | <b>1,242</b> |                           | <b>3,344</b> |
|   | %                           | %                  | %                                       | %               | %            |                           | %            |
| Share of HSBC's profit before tax   | 2.5                         | 4.2                | 7.8                                     | 0.4             | 8.7          |                           | 23.6         |
| Cost efficiency ratio   | 68.9                        | 39.3               | 34.1                                    | 48.6            | 22.8         |                           | 39.8         |

**Balance sheet data<sup>2</sup>**

|  | US\$m  | US\$m  | US\$m   | US\$m | US\$m | US\$m   |
|--|--------|--------|---------|-------|-------|---------|
| Loans and advances to customers (net)  | 31,768 | 25,996 | 27,575  | 2,716 | 119   | 88,174  |
| Total assets   | 38,544 | 31,553 | 116,396 | 6,791 | 7,839 | 201,123 |
| Customer accounts  | 44,686 | 28,803 | 44,126  | 9,092 | 752   | 127,459 |
| Loans and advances to banks (net) <sup>3</sup>   |        |        | 28,663  |       |       |         |
| Trading assets, financial instruments designated at fair value, and financial investments <sup>3</sup> |        |        | 46,674  |       |       |         |
| Deposits by banks <sup>3</sup>   |        |        | 12,860  |       |       |         |

*For footnotes, see page 51.*

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HSBC HOLDINGS PLC

**Business Review** (continued)

Profit before tax and balance sheet data by customer group and global business (continued)

Half-year to 30 June 2006

| Rest of Asia-Pacific (including the Middle East)                                     | Personal           | Commercial | Corporate,                   | Private    | Other      | Inter-              | Total        |
|--|--------------------|------------|------------------------------|------------|------------|---------------------|--------------|
|  | Financial Services | Banking    | Investment Banking & Markets | Banking    |            | segment elimination |              |
|  | US\$m              | US\$m      | US\$m                        | US\$m      | US\$m      | US\$m               | US\$m        |
| Net interest income  | 720                | 400        | 405                          | 18         | 33         | (97)                | 1,479        |
| Net fee income   | 259                | 162        | 322                          | 39         | 3          |                     | 785          |
| Trading income/(expense) excluding net interest income                               | 28                 | 43         | 376                          | 43         | (9)        |                     | 481          |
| Net interest income/(expense) on trading activities                                  | 1                  |            | (28)                         |            |            | 97                  | 70           |
| Net trading income/(expense)   | 29                 | 43         | 348                          | 43         | (9)        | 97                  | 551          |
| Net income/(expense) from financial instruments designated at fair value             | (9)                |            | 1                            |            | 3          |                     | (5)          |
| Gains less losses from financial investments   |                    | 2          | 28                           | (1)        | (2)        |                     | 27           |
| Dividend income  |                    |            |                              |            |            |                     |              |
| Net earned insurance premiums  | 77                 | 12         |                              |            |            |                     | 89           |
| Other operating income   | 11                 | 4          | 43                           | 1          | 273        | (44)                | 288          |
| <b>Total operating income</b>  | <b>1,087</b>       | <b>623</b> | <b>1,147</b>                 | <b>100</b> | <b>301</b> | <b>(44)</b>         | <b>3,214</b> |
| Net insurance claims <sup>1</sup>  | (57)               | (6)        |                              |            |            |                     | (63)         |
| Net operating income before loan impairment charges and other credit risk provisions | 1,030              | 617        | 1,147                        | 100        | 301        | (44)                | 3,151        |
| Loan impairment (charges)/ recoveries and other credit risk provisions               | (289)              | 19         | (1)                          |            |            |                     | (271)        |
| <b>Net operating income</b>  | <b>741</b>         | <b>636</b> | <b>1,146</b>                 | <b>100</b> | <b>301</b> | <b>(44)</b>         | <b>2,880</b> |
| Total operating expenses   | (707)              | (252)      | (400)                        | (52)       | (242)      | 44                  | (1,609)      |
| Operating profit   | 34                 | 384        | 746                          | 48         | 59         |                     | 1,271        |
| Share of profit in associates and joint ventures                                     | 171                | 114        | 93                           |            | 8          |                     | 386          |
| <b>Profit before tax</b>   | <b>205</b>         | <b>498</b> | <b>839</b>                   | <b>48</b>  | <b>67</b>  |                     | <b>1,657</b> |
|  | %                  | %          | %                            | %          | %          |                     | %            |

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|  |        |        |        |       |       |         |
|--|--------|--------|--------|-------|-------|---------|
| Share of HSBC's profit before tax  | 1.6    | 4.0    | 6.7    | 0.4   | 0.5   | 13.2    |
| Cost efficiency ratio  | 68.6   | 40.8   | 34.9   | 52.0  | 80.4  | 51.1    |
| Balance sheet data <sup>2</sup>  |        |        |        |       |       |         |
|  | US\$m  | US\$m  | US\$m  | US\$m | US\$m | US\$m   |
| Loans and advances to customers (net)  | 28,879 | 19,784 | 23,589 | 2,460 | 127   | 74,839  |
| Total assets   | 32,806 | 23,737 | 97,571 | 6,299 | 8,444 | 168,857 |
| Customer accounts  | 34,932 | 20,436 | 34,350 | 7,399 | 142   | 97,259  |
| Loans and advances to banks (net) <sup>3</sup>   |        |        | 20,652 |       |       |         |
| Trading assets, financial instruments designated at fair value, and financial investments <sup>3</sup> |        |        | 31,368 |       |       |         |
| Deposits by banks <sup>3</sup>   |        |        | 8,527  |       |       |         |

For footnotes, see page 51.

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Half-year to 31 December 2006

| Rest of Asia-Pacific (including the Middle East)  | Personal Financial Services | Commercial Banking | Corporate, Investment Banking & Markets | Private Banking | Other        | Inter-segment elimination | Total          |
|---|-----------------------------|--------------------|---|-----------------|--------------|---------------------------|----------------|
|   | US\$m                       | US\$m              | US\$m                                   | US\$m           | US\$m        | US\$m                     | US\$m          |
| Net interest income   | 800                         | 448                | 397                                     | 17              | 28           | (122)                     | 1,568          |
| Net fee income  | 265                         | 168                | 366                                     | 29              | 9            |                           | 837            |
| Trading income excluding net interest income  | 33                          | 43                 | 341                                     | 31              | 6            |                           | 454            |
| Net interest income/(expense) on trading activities   | (1)                         |                    | 28                                      |                 | 27           | 122                       | 176            |
| Net trading income  | 32                          | 43                 | 369                                     | 31              | 33           | 122                       | 630            |
| Net income from financial instruments designated at fair value                              | 68                          | 4                  | 3                                       |                 | 9            |                           | 84             |
| Gains less losses from financial investments  | 2                           |                    | 10                                      |                 | 2            |                           | 14             |
| Dividend income   |                             |                    | 1                                       |                 | 4            |                           | 5              |
| Net earned insurance premiums   | 71                          | 14                 |   |                 |              |                           | 85             |
| Other operating income  | 97                          | 16                 | 18                                      | (1)             | 394          | (47)                      | 477            |
| <b>Total operating income</b>   | <b>1,335</b>                | <b>693</b>         | <b>1,164</b>                            | <b>76</b>       | <b>479</b>   | <b>(47)</b>               | <b>3,700</b>   |
| Net insurance claims <sup>1</sup>   | (123)                       | (5)                |   |                 | (1)          |                           | (129)          |
| <b>Net operating income before loan impairment charges and other credit risk provisions</b> | <b>1,212</b>                | <b>688</b>         | <b>1,164</b>                            | <b>76</b>       | <b>478</b>   | <b>(47)</b>               | <b>3,571</b>   |
| Loan impairment (charges)/recoveries and other credit risk provisions                       | (256)                       | 10                 | 6                                       |                 | (1)          |                           | (241)          |
| <b>Net operating income</b>   | <b>956</b>                  | <b>698</b>         | <b>1,170</b>                            | <b>76</b>       | <b>477</b>   | <b>(47)</b>               | <b>3,330</b>   |
| <b>Total operating expenses</b>   | <b>(886)</b>                | <b>(302)</b>       | <b>(469)</b>                            | <b>(44)</b>     | <b>(285)</b> | <b>47</b>                 | <b>(1,939)</b> |
| <b>Operating profit</b>   | <b>70</b>                   | <b>396</b>         | <b>701</b>                              | <b>32</b>       | <b>192</b>   |                           | <b>1,391</b>   |
| Share of profit in associates and joint ventures  | 202                         | 140                | 109                                     |                 | 28           |                           | 479            |
| <b>Profit before tax</b>  | <b>272</b>                  | <b>536</b>         | <b>810</b>                              | <b>32</b>       | <b>220</b>   |                           | <b>1,870</b>   |
|   | %                           | %                  | %                                       | %               | %            |                           | %              |
| Share of HSBC's profit before tax   | 2.8                         | 5.6                | 8.5                                     | 0.3             | 2.3          |                           | 19.5           |
| Cost efficiency ratio   | 73.1                        | 43.9               | 40.3                                    | 57.9            | 59.6         |                           | 54.3           |
| Balance sheet data <sup>2</sup>   | US\$m                       | US\$m              | US\$m                                   | US\$m           | US\$m        |                           | US\$m          |
| Loans and advances to customers (net)   | 28,911                      | 21,912             | 24,311                                  | 2,313           | 127          |                           | 77,574         |
| Total assets  | 35,317                      | 26,335             | 93,605                                  | 6,476           | 5,935        |                           | 167,668        |
| Customer accounts   | 38,557                      | 24,228             | 36,623                                  | 8,929           | 658          |                           | 108,995        |

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|  |        |
|--|--------|
| Loans and advances to banks (net) <sup>3</sup>   | 22,171 |
| Trading assets, financial instruments designated at fair value, and financial investments <sup>3</sup> | 36,580 |
| Deposits by banks <sup>3</sup>   | 9,849  |

- 1 *Net insurance claims incurred and movement in policyholders' liabilities.*
- 2 *Third party only.*
- 3 *These assets and liabilities were significant to Corporate, Investment Banking and Markets.*

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HSBC HOLDINGS PLC

**Business Review** (continued)**North America**

Profit/(loss) before tax by country within customer groups and global businesses

|  | Personal<br>Financial<br>Services<br>US\$m | Commercial<br>Banking<br>US\$m | Corporate,<br>Investment<br>Banking &<br>Markets<br>US\$m | Private<br>Banking<br>US\$m | Other<br>US\$m | Total<br>US\$m |
|--|--|--------------------------------|---|-----------------------------|----------------|----------------|
| <b>Half-year to 30 June 2007</b>             |  |                                |   |                             |                |                |
| United States                                | 1,336                                      | 215                            | 292   | 50                          | (44)           | 1,849          |
| Canada                                       | 145  | 222                            | 120   | 4                           | 2              | 493            |
| Bermuda                                      | 7  | 40                             | 24  | 6                           | 16             | 93             |
|  | <u>1,488</u>                               | <u>477</u>                     | <u>436</u>  | <u>60</u>                   | <u>(26)</u>    | <u>2,435</u>   |
| <b>Half-year to 30 June 2006<sup>1</sup></b> |  |                                |   |                             |                |                |
| United States                                | 2,886                                      | 206                            | 273   | 37                          | (145)          | 3,257          |
| Canada                                       | 122  | 220                            | 49  |                             | 2              | 393            |
| Bermuda                                      | 9  | 38                             | 25  | 1                           | 16             | 89             |
| Other  |  |                                | 2   |                             |                | 2              |
|  | <u>3,017</u>                               | <u>464</u>                     | <u>349</u>  | <u>38</u>                   | <u>(127)</u>   | <u>3,741</u>   |
| <b>Half-year to 31 December 2006</b>         |  |                                |   |                             |                |                |
| United States                                | 242  | 236                            | (74)  | 70                          | (119)          | 355            |
| Canada                                       | 131  | 217                            | 140   |                             | 15             | 503            |
| Bermuda                                      | 1  | 40                             | 6   | 6                           | 13             | 66             |
| Other  |  |                                | 2   |                             | 1              | 3              |
|  | <u>374</u>                                 | <u>493</u>                     | <u>74</u>   | <u>76</u>                   | <u>(90)</u>    | <u>927</u>     |

Loans and advances to customers (net) by country

|               | Half-year to             |                                       |                              |
|---------------|--------------------------|---------------------------------------|------------------------------|
|               | 30 June<br>2007<br>US\$m | 30 June<br>2006 <sup>1</sup><br>US\$m | 31 December<br>2006<br>US\$m |
| United States | 233,592                  | 227,690                               | 236,188                      |
| Canada        | 45,510                   | 39,181                                | 39,584                       |
| Bermuda       | 2,193                    | 1,999                                 | 2,215                        |



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|                |         |         |
|----------------|---------|---------|
| <b>281,295</b> | 268,870 | 277,987 |
|----------------|---------|---------|

Customer accounts by country

Half-year to

|               | <b>30 June<br/>2007<br/>US\$m</b> | 30 June<br>2006 <sup>1</sup><br>US\$m | 31 December<br>2006<br>US\$m |
|---------------|-----------------------------------|---------------------------------------|------------------------------|
| United States | <b>93,325</b>                     | 86,053                                | 84,560                       |
| Canada        | <b>32,744</b>                     | 28,989                                | 28,668                       |
| Bermuda       | <b>8,328</b>                      | 8,464                                 | 7,694                        |
|               | <b>134,397</b>                    | 123,506                               | 120,922                      |

1 In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

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## Profit before tax

|   | Half-year to             |                                       |                              |
|---|--------------------------|---------------------------------------|------------------------------|
|   | 30 June<br>2007<br>US\$m | 30 June<br>2006 <sup>1</sup><br>US\$m | 31 December<br>2006<br>US\$m |
| <b>North America</b>  |                          |                                       |                              |
| Net interest income   | 7,307                    | 6,996                                 | 7,272                        |
| Net fee income  | 2,904                    | 2,312                                 | 2,454                        |
| Net trading income  | 622                      | 959                                   | 399                          |
| Net income/(expense) from financial instruments designated at fair value                    | 81                       | 24                                    | (87)                         |
| Gains less losses from financial investments  | 53                       | 40                                    | 18                           |
| Dividend income   | 64                       | 39                                    | 46                           |
| Net earned insurance premiums   | 231                      | 238                                   | 254                          |
| Other operating income  | 342                      | 365                                   | 557                          |
| <b>Total operating income</b>   | <b>11,604</b>            | <b>10,973</b>                         | <b>10,913</b>                |
| Net insurance claims incurred and movement in policyholders' liabilities                    | (124)                    | (117)                                 | (142)                        |
| <b>Net operating income before loan impairment charges and other credit risk provisions</b> | <b>11,480</b>            | <b>10,856</b>                         | <b>10,771</b>                |
| Loan impairment charges and other credit risk provisions                                    | (3,820)                  | (2,172)                               | (4,624)                      |
| <b>Net operating income</b>   | <b>7,660</b>             | <b>8,684</b>                          | <b>6,147</b>                 |
| Total operating expenses  | (5,235)                  | (4,974)                               | (5,219)                      |
| <b>Operating profit</b>   | <b>2,425</b>             | <b>3,710</b>                          | <b>928</b>                   |
| Share of profit in associates and joint ventures  | 10                       | 31                                    | (1)                          |
| <b>Profit before tax</b>  | <b>2,435</b>             | <b>3,741</b>                          | <b>927</b>                   |
|   | %                        | %                                     | %                            |
| Share of HSBC's profit before tax   | 17.2                     | 29.9                                  | 9.7                          |
| Cost efficiency ratio   | 45.6                     | 45.8                                  | 48.5                         |
| Period-end staff numbers (full-time equivalent)   | 56,693                   | 54,884                                | 55,642                       |

Balance sheet data<sup>2</sup>

|   | US\$m   | US\$m   | US\$m   |
|---|---------|---------|---------|
| Loans and advances to customers (net)   | 281,295 | 268,870 | 277,987 |
| Loans and advances to banks (net)   | 18,643  | 16,753  | 17,865  |
| Trading assets, financial instruments designated at fair value, and financial investments | 149,004 | 141,631 | 145,700 |
| Total assets  | 519,693 | 495,895 | 511,190 |
| Deposits by banks   | 13,043  | 10,026  | 11,484  |
| Customer accounts   | 134,397 | 123,506 | 120,922 |

1 In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

2 Third party only.

## Economic briefing

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**US** economic growth slowed in the early part of 2007 but subsequently appeared to regain some momentum. Annualised real growth rates of 2 per cent and 2.5 per cent were recorded in GDP and consumer spending, respectively, in the first half of the year. The volume of residential investment dropped at an annualised rate of 12.8 per cent in the first part of 2007, however. Home building and home sales continued to fall, and home price appreciation slowed, with some regions experiencing outright declines in house prices. Employment conditions were characterised by steady job gains and an average unemployment rate of 4.5 per cent.

In June, total CPI inflation was 2.7 per cent year-on-year, reflecting higher food and fuel prices. However, core CPI (excluding food and energy) was 2.2 per cent, partly due to the general slowdown in the residential property market. Having last raised interest rates in June 2006, the Federal Reserve Board left the federal funds rate unchanged at 5.25 per cent throughout the first half of 2007.

**Canada** s economic growth in early 2007 was solid, with annualised real GDP growth of 3.7 per cent in the first quarter. Strong housing market activity helped boost consumer spending on goods and services, which rose by 3.9 per cent annualised in the first quarter. Residential investment spending

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HSBC HOLDINGS PLC

**Business Review** (continued)

rose by 7.5 per cent annualised in the first quarter, the first increase in a year. By contrast, investment in non-residential construction slowed while machinery and equipment investment fell for the first time since 2002. Core inflation in June rose to 2.2 per cent, the highest since March 2003. The Canadian dollar appreciated by more than 8 per cent against the US dollar in the first half of the year, boosted by strong demand and firm commodity prices. The Bank of Canada left the overnight target rate unchanged at 4.25 per cent throughout the period but raised rates by 25 basis points to 4.5 per cent in early July.

## Review of business performance

HSBC's operations in North America reported a pre-tax profit of US\$2,435 million compared with US\$3,741 million in the first half of 2006, a decrease of 35 per cent. Compared with the second half of 2006, profit before tax improved significantly.

On an underlying basis, pre-tax profits declined by 35 per cent. Underlying net operating income before loan impairment charges was 6 per cent higher, mainly as a result of increased net fee income from the card services business within Personal Financial Services. This was more than offset by increased loan impairment charges in the mortgage services and consumer lending businesses as a result of higher delinquencies. In part, this reflected the combination of higher lending and the deterioration in credit quality within the mortgage services business. It also reflected the abnormally low level of impairment recognised in the first half of 2006 as a consequence of bankruptcy law changes in the fourth quarter of 2005. A rise in Commercial Banking income, driven by balance sheet growth, covered increased expenses incurred in support of regional and business expansion. CIBM's revenue increased by 8 per cent, notwithstanding lower balance sheet management income. In Private Banking, revenues increased, driven by a rise in customer numbers.

The following commentary is on an underlying basis.

**Personal Financial Services** generated a pre-tax profit of US\$1,488 million, down by 51 per cent on the first half of 2006 but a substantial recovery of 301 per cent compared with the second half of the year. The combination of higher loan impairment charges, increased collection expenses in mortgage services and higher marketing expenditure in support of business expansion in the consumer finance company and retail bank, outweighed the rise in revenues from balance sheet growth and improved fee income.

In the US, pre-tax profit declined by 54 per cent to US\$1,336 million due to higher loan impairment charges and the effect of lower asset growth, largely driven by HSBC's planned reduction in mortgage balances in the mortgage services business, discussed more fully below. The rise in loan impairment charges partly reflected asset growth and portfolio seasoning, but was also due to deterioration in sub-prime mortgages originated through the mortgage services channel. The credit quality of second lien and certain portions of first lien loans originated during 2005 and 2006 continued to deteriorate against historical experience, but remained broadly in line with management expectations established at the beginning of the year. The rate of increase in delinquency slowed compared with full year 2006 delinquencies, as management initiatives on collection took effect.

In Canada, profit before tax grew by 18 per cent to US\$145 million, reflecting strong asset and deposit growth and a gain on a sale of shares in the Montreal Exchange.

Net interest income grew by 1 per cent to US\$6,545 million. In the US, net interest income was marginally higher. Lending balances rose, with notably strong growth in the credit card portfolio. Mortgage balances increased only modestly, as growth in this area was restricted by steps taken to reduce HSBC's exposure to correspondent mortgages acquired through the mortgage services business. Also, in March 2007 HSBC made the decision to stop purchasing new originations from correspondents. Deposit balances grew too, but liability spreads declined which, together with a narrowing of asset spreads from higher funding costs, largely offset the benefits of balance sheet growth.

Average deposit balances were 25 per cent higher, driven by the continued success of the online savings product. During the first half of 2007, a special promotional rate offer led to 149,000 new account openings and attracted US\$4.6 billion of new balances. By 30 June 2007, online savings balances through HSBC Direct had reached US\$12.0 billion and customer numbers exceeded 560,000 with US\$7.1 billion of new average balances added in the previous 12 months. Growth in Premier, where customer numbers rose by 21 per cent, together with new balances generated from the ongoing branch expansion programme, contributed further to the rise. The financial benefit of higher balances was moderated by the use of competitive pricing to increase customer acquisition, and a change in product mix as customers migrated to higher

yielding deposits.

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The slowdown in the US housing market noted in 2006 continued into 2007, evidenced by the deterioration in key indicators such as sales of new and existing homes and levels of house building activity. Average mortgage balances rose by 2 per cent to US\$124.4 billion. Average mortgage balances generated through the consumer lending branch network rose by 20 per cent, primarily driven by increased sales of these branch-based products and lower levels of repayments. The US\$2.5 billion Champion mortgage portfolio purchased from KeyBank, NA in the final quarter of 2006 also contributed to the rise.

In the mortgage services correspondent business, average balances fell by 4 per cent to US\$46.8 billion, reflecting HSBC's planned strategy to reduce balances in this business. As part of this, HSBC took a decision in March 2007 to stop purchasing new loans from correspondents. In addition, in the first half of 2007, a total of US\$2.7 billion of loans which did not include any loans that were 30 days or more delinquent were sold which, along with normal loan repayments, contributed to the decrease in balances.

Prime mortgage balances also continued to fall as HSBC sold down the majority of new loan originations to government-sponsored enterprises and private investors, and elected not to replace portfolios being run-off. Changes in product mix in the mortgage portfolio, reflecting a higher proportion of non-prime mortgages, together with re-pricing initiatives, led to improved yields but, despite this, spreads declined as a result of higher funding costs.

Average credit card balances rose by 13 per cent, partly due to strong organic growth in the core and Metris credit card portfolios from increased marketing. The upgrading and re-launch of the Union Privilege product, growth in the General Motors' programme and lower levels of repayments in these portfolios contributed further to the increase in balances. Improved yields from repricing and a change in mix to higher levels of non-prime balances offset the impact of higher funding costs, with the subsequent improvement in margins augmenting the benefits of volume growth.

In retail services, average balances rose by 5 per cent, driven by a combination of organic growth and the launch of new co-branded relationships, notably with Best Buy and Saks Fifth Avenue. This benefit compensated for reduced spreads, as a large portion of the book priced at fixed rates was affected by higher funding costs as interest rates rose. Spreads were also reduced by changes in the product mix.

Rising interest rates, higher fuel prices and reductions in the level of incentive programmes offered by car manufacturers led to an almost 5 per cent decline in total industry sales from franchised dealerships. Notwithstanding this, HSBC grew average vehicle loan balances by 6 per cent, mainly from the successful development of the consumer direct channel, as sales generated online and through direct mailings increased by over 50 per cent. The strengthening of relationships with active dealers and higher refinancing volumes, which were driven by improved pricing and increased operational capacity, also contributed to the overall increase. Spreads declined slightly, reflecting changes in product mix from the dealer channel towards near-prime customers and higher funding costs.

Personal non-credit card average loan balances rose by 6 per cent, as a result of targeted direct mail campaigns and higher average loan amounts per customer.

In Canada, net interest income rose by 17 per cent due to lending and deposit growth, partly offset by reduced asset and deposit spreads.

Average deposit balances in Canada grew by 11 per cent, as HSBC continued to improve its high rate savings and direct banking propositions with a new high-yielding online savings account. Together, these successfully generated over US\$906 million of incremental balances, of which US\$98 million came from new customers to HSBC. The consequent change in product mix, combined with competitive pricing pressures, led to reduced deposit spreads, partly offsetting the benefit of balance growth.

Average lending balances were 15 per cent higher, as strong economic conditions fuelled customer demand for credit assumed through cards and personal loans. A strong Canadian housing market and ongoing branch expansion in consumer finance led to higher mortgage balances. Motor vehicle balances grew from the expansion of the motor finance programme. The greater proportion of secured lending balances and competitive market conditions resulted in a narrowing of asset spreads which partly offset the income benefits from asset growth.

Net fee income grew by 28 per cent to US\$2,332 million, largely in the US credit cards and retail services businesses, reflecting volume growth and better cross-selling of enhancement services.

In the US retail bank's mortgage business, net fee income declined. Although increased volumes of mortgage loans serviced led to higher gross servicing fees, this was more than offset by higher



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HSBC HOLDINGS PLC

## Business Review (continued)

amortisation charges and lower releases of impairment allowances on mortgage servicing rights. In the taxpayer financial services business, a change in contractual terms led to additional payments being made to business partners which resulted in an 8 per cent fall in fee income.

Trading income went from a profit of US\$215 million in the first half of 2006 to a loss of US\$97 million in the first half of 2007. The 2007 results reflected lower market prices and a decline in market liquidity for wholesale mortgages which affected the Decision One mortgage business. By contrast, the results in 2006 benefited from significantly higher volumes of loans sold in a better market environment. The Decision One trading portfolio at 30 June 2007 has been reduced from the level held at the end of 2006.

The reduction in gains less losses from financial instruments reflected the non-recurrence of the proceeds related to the MasterCard Incorporated IPO. This was partly mitigated by a gain on the sale of shares held in the Montreal Exchange.

Other operating income declined by 26 per cent, primarily from losses arising on asset sales following branch closures in the mortgage services business, along with lower income in the retail services business. This was partly offset by lower incremental losses on the sale of foreclosed assets, reflecting the establishment of substantial reserves in the latter part of 2006, and a gain following the sale and leaseback of a building previously owned by HSBC's US bank.

Loan impairment charges and other credit risk provisions rose by 78 per cent to US\$3,774 million.

In the US, loan impairment charges rose by 80 per cent. This reflected asset growth and portfolio seasoning in the consumer lending and cards businesses, as well as the deterioration noted above in sub-prime mortgages originated within the mortgage services business. Impairment charges in the corresponding period in 2006 were also abnormally low from the effects of changes in bankruptcy legislation. Although 2007 bankruptcy levels were higher than the equivalent period in 2006, filings remained below historical trends.

In the mortgage services business, loan impairment charges increased significantly, driven by higher delinquency and losses, largely as a result of the affected 2005 and 2006 originations

progressing to various stages of delinquency and then to write-off. Although delinquencies rose, this rate of growth slowed during 2007, broadly in line with management expectations. Numerous risk mitigation efforts were implemented relating to the affected components of the mortgage services portfolio. These included enhanced segmentation and analytics in order to identify the higher risk portions of the portfolio and increased levels of collections activity. In the second half of 2006, HSBC slowed growth in this portion of the portfolio by implementing re-pricing initiatives in selected origination segments and tightening underwriting criteria, especially for second lien, stated income, and lower credit scoring segments. In March this year, HSBC announced the decision to discontinue correspondent channel acquisitions in this business. The Decision One mortgage broker business was also restructured in light of significant changes in the wholesale mortgage industry. Loan processing and underwriting functions were centralised and the number of operating centres reduced from 17 to 2. Portions of the mortgage services portfolio are expected to remain under pressure as the 2005 and 2006 originations further progress to various stages of delinquency and ultimately to write-off.

Mortgage services' loan impairment allowances of US\$2.1 billion at 30 June 2007 were consistent with the balance at 31 December 2006 and reflect the best estimate of losses in the portfolio. The balance at 30 June 2007 was broadly in line with the end of 2006, as a significant portion of interest rate resets on first lien adjustable rate mortgages (ARMs), including second lien customers with underlying first lien ARMs, have yet to occur and HSBC remains cautious about losses inherent in this portfolio due to economic factors beyond HSBC's control. The loan impairment charge for mortgage services was US\$760 million in the period, with write-offs net of recoveries of US\$680 million.

The consumer lending business also experienced higher loan impairment charges, from balance growth, portfolio seasoning and increased loss severity on second lien loans acquired between 2004 and the third quarter of 2006. A more normalised level of bankruptcy filings after the exceptionally low levels experienced in 2006 also contributed to the increase.

An 84 per cent rise in credit card loan impairment charges resulted from balance growth, an increase in bankruptcies following the abnormally low levels seen in 2006, and changes in the product mix as sub-prime and near-prime balances rose faster than prime loans.





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In Canada, loan impairment charges rose by 25 per cent as a result of balance growth and higher delinquency rates in credit cards and vehicle financing portfolios.

Operating expenses grew by 3 per cent to US\$3,783 million. In the US, costs increased by 3 per cent. Staff costs were higher following the recruitment in the consumer finance business to support asset growth and increased collections activity in mortgage services. Employee severance costs grew, partly reflecting the effects of terminating mortgage purchases from correspondents and the restructuring of Decision One. These increases were partly offset by reduced incentive costs, largely attributable to lower originations in mortgage services.

The rise in non-staff costs was mostly due to increased marketing expenditure on growing the core and Metris credit card portfolios, and promoting the co-branded portfolio in retail services. Marketing costs in the retail bank grew from branding initiatives at the John F Kennedy International and La Guardia airports, and expansion of the branch network. Several campaigns to promote online savings, mortgages and card products also contributed to the increase. Other administrative and support expenses rose, fuelled by higher business volumes. Higher costs were also incurred following a rise in the number of foreclosed properties.

Operating expenses increased by 11 per cent in Canada. Staff costs rose due to branch expansion, from ongoing investments in new initiatives and to support revenue growth. Higher marketing costs reflected various promotions, principally relating to the direct savings product and brand awareness campaigns. Other administrative and support costs grew in response to higher levels of transactions, and from the development of a new customer website.

**Commercial Banking** s pre-tax profits of US\$477 million rose by 3 per cent compared with the first half of 2006. In the US, significant resources were dedicated to expanding various commercial lending businesses and regional offices, which resulted in a rise in loan and deposit balances. The growth of the branch network and consequent rise in staffing levels in 2006, the expansion of the range of loan and deposit products offered to small businesses and mid-market commercial customers, and increased marketing efforts resulted in average commercial loans and deposits being 2 per cent and 20 per cent higher, respectively, in the first six months of 2007 compared with the same period in 2006. HSBC Bank USA launched a Green Campaign targeting new customers with a package

of incentives for those switching to online bill payments.

In Canada, profits before tax also rose. Balance sheet growth was strong and credit fees improved.

Net interest income increased by 16 per cent to US\$740 million. In the US, the 15 per cent rise was driven by strong growth from small, micro and medium sized business customers. This reflected the continued efforts made by HSBC to further develop its operations through a combination of increased geographical distribution and new products designed to cater for small and medium business customers, supported by the recruitment of additional sales staff and higher levels of marketing activity. The restructuring of the branch sales force dedicated to small and micro business customers also contributed to the rise in net interest income.

Average deposit balances in the US rose by 20 per cent, reflecting geographical expansion, marketing campaigns and a greater emphasis on generating deposits from small and micro business customers. Continued migration to higher yielding products led to a change in product mix, with the subsequent reduction in spreads partly offsetting the income benefits from volume growth.

Lending balances in the US were 2 per cent higher. Geographical expansion continued as 10 new branches were opened which contributed to loan growth from small and micro business customers. A greater focus on attracting higher volumes from mid-market customers, particularly from the new offices opened in recent years, also contributed to the overall increase. The rate of overall balance growth, however, was subdued following a tightening of underwriting standards for certain loans made to small and micro business customers and a slowdown in the commercial real estate market. Lending spreads narrowed, partly offsetting the income benefits from volume growth.

In Canada, net interest income increased by 16 per cent. Average deposit balances rose by 22 per cent, attributable to a combination of higher payments and cash management balances following significant investments made to develop new products, and the acquisition of new customers. There was also an improvement in deposit spreads.

Demand for lending remained strong, reflecting favourable economic conditions as average lending balances rose by 18 per cent. There was particularly robust growth in non-real estate lending as this was promoted ahead of real estate in order to meet regulatory guidelines to limit overall exposure to real



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HSBC HOLDINGS PLC

## Business Review (continued)

estate loans. Lending spreads remained in line with 2006.

In Bermuda, net interest income increased by 24 per cent. Deposit balances declined but this was more than offset by improved liability spreads in a rising interest rate environment. Average lending balances rose by 29 per cent, reflecting strong demand for commercial real estate lending.

Net fee income rose by 1 per cent to US\$152 million. In the US, fee income was 6 per cent higher, reflecting geographical and business expansion initiatives which led to increased card and service deposit fees. A rise in the level of foreign exchange transactions resulted in improved fees from mid-market customers. Real estate servicing fees increased, following a new initiative whereby corporate real estate loans originated by HSBC were sold with servicing rights retained to Fannie Mae, a government-sponsored agency. By contrast, commercial mortgage syndication fees declined, due to lower volumes and cyclical market conditions.

In Canada, fee income fell, but this was mainly attributable to the adverse effect of a fair value adjustment on guarantee fees, and a reclassification of fees related to the Canadian Immigrant Investor Programme to the Personal Financial Services segment. Excluding these factors, fee income rose, primarily driven by higher credit fees.

Loan impairment charges of US\$46 million were 48 per cent, or US\$15 million, higher than in the first half of 2006. In the US, the rise reflected asset growth and a return to a credit environment more in keeping with historical trends. Strong asset growth led to higher impairment charges in Canada, but credit conditions remained favourable in the robust economic climate, consequently charges remained low compared with historical levels. In Bermuda, the increase in impairment charges was due to the non-recurrence of a corporate debt recovery.

Operating expenses increased by 14 per cent to US\$443 million. In the US, expenses grew by 20 per cent, as geographical and business expansion led to increased staff and administrative costs. The 3 per cent rise in Canada was attributable to higher staff costs to support growth initiatives, annual pay rises and increased bonus costs from improved revenues.

Income from associates fell, following the non-recurrence of revaluation gains. Excluding this, income from associates rose, driven by an improved performance of HSBC's private equity investments in Canada.

**Corporate, Investment Banking and Markets** in North America, reported a pre-tax profit of US\$436 million, which represented 10 per cent of the global business's pre-tax profits, and a rise of 25 per cent compared with the first half of 2006. Total operating income of US\$1,197 million was 8 per cent higher than in the first half of 2006. In 2005 and 2006, targeted expansion of the sales and trading operations and various treasury activities resulted in a wider range of product offerings, increased marketing of those products, and an expanded infrastructure to support business growth. As a result of these initiatives, corporate loans, trading assets and deposits in the US increased in the first six months of 2007 compared with the same period in 2006.

The increase in net interest income was driven by lower funding costs and higher net interest income from payments and cash management activities, reflecting the benefit of growing deposit balances. Balance sheet management activities continued to be adversely affected by a rise in short-term interest rates and a flat yield curve.

Net fee income was in line with the first half of 2006. Payments and cash management and securities recorded a 21 per cent increase in transaction fees as higher volumes were generated from a wider range of product offerings and assets under custody grew significantly since the end of 2006.

Net trading income increased by 7 per cent. Derivatives trading revenue from structured products increased by 86 per cent due to a broader product offering in structured credit and emerging market derivatives. Credit and rates activity was adversely affected by widening credit spreads, while the metals business reported a decline as customer volumes decreased against the backdrop of relatively lower precious metals prices. Foreign exchange activities and revenues remained strong throughout 2007, driven by the continued weakening of the US dollar.

The benign corporate credit environment experienced in recent years continued and a small release of impairment allowances was reported.

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Operating expenses were broadly in line with the first half of 2006 and some 12 per cent lower than in the second half of the year.

**Private Banking** reported pre-tax profits of US\$60 million, an increase of 54 per cent compared with the first half of 2006. The cost efficiency ratio of 74.2 per cent was 2.8 per cent worse than the comparable prior period. Encouraging growth in revenues was driven by strong increases in net interest income and fees, buoyed by a rise in high net

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worth customers. This was supported by increased referrals from within the wider HSBC group compared with the first half of 2006. Loan impairment charges fell significantly, improving by US\$18 million to US\$12 million.

Net interest income of US\$117 million was 15 per cent higher than in the first half of 2006, driven by strong balance sheet growth, with a slight reduction in spreads. Growth in lending balances was driven by the Tailored Mortgage Solutions product, where balances reached US\$364 million, while deposit inflows from offshore clients contributed to growth in customer accounts. Overall, average deposit balances rose by 20 per cent and average lending balances increased by 13 per cent.

Demand from clients for HSBC's discretionary managed products and the Universal Investor insurance product, which wraps an investment portfolio and facilitates risk management, contributed to an 18 per cent increase in net fee income, which reached US\$140 million.

Client assets grew by 4 per cent to US\$45 billion. Very strong demand from clients for the discretionary managed SIS and CIS products saw the value of balances in the Investment Solutions product range rise by 41 per cent. Client appetite for fund and alternative investment products remained strong.

Loan impairment charges were 60 per cent lower than in the first half of 2006. In both years, charges predominantly related to isolated single credit issues.

Operating expenses were US\$207 million, with growth of 20 per cent increasing at a slightly faster rate than operating income. Cost growth was driven by performance-related remuneration, in addition to increased staff numbers, largely client facing, to support the expansion of the business.

**Other** included fair value movements of US\$81 million on HSBC's own debt in issue and related swaps, which were largely a consequence of a widening of credit spreads. Costs at HSBC Technology USA Inc, which provides technology support to HSBC's North American subsidiaries, rose by 17 per cent to US\$673 million, with recharges reported as Other operating income rising by 10 per cent to US\$684 million.

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HSBC HOLDINGS PLC

**Business Review** (continued)

Profit/(loss) before tax and balance sheet data by customer group and global business

## Half-year to 30 June 2007

| North America   | Personal<br>Financial<br>Services<br>US\$m | Commercial<br>Banking<br>US\$m | Corporate,<br>Investment<br>Banking &<br>Markets<br>US\$m | Private<br>Banking<br>US\$m | Other<br>US\$m | Inter-<br>segment<br>elimination<br>US\$m | Total<br>US\$m |
|---|--|--------------------------------|---|-----------------------------|----------------|---|----------------|
| Net interest income/(expense)   | 6,545                                      | 740                            | 202   | 117                         | (18)           | (279)                                     | 7,307          |
| Net fee income/(expense)  | 2,332                                      | 152                            | 320   | 140                         | (40)           |   | 2,904          |
| Trading income/(expense) excluding<br>net interest income   | (184)                                      | 3                              | 483   | 6                           | (62)           |   | 246            |
| Net interest income on trading<br>activities  | 87   |                                | 10  |                             |                | 279                                       | 376            |
| Net trading income/(expense)  | (97)                                       | 3                              | 493   | 6                           | (62)           | 279                                       | 622            |
| Net income from financial instruments<br>designated at fair value                                   |  |                                | 3   |                             | 78             |   | 81             |
| Gains less losses from financial<br>investments   | 9  |                                | 42  | 2                           |                |   | 53             |
| Dividend income   | 35   | 1                              | 28  |                             |                |   | 64             |
| Net earned insurance premiums   | 231  |                                |   |                             |                |   | 231            |
| Other operating income  | 114  | 58                             | 109   | 14                          | 735            | (688)                                     | 342            |
| <b>Total operating income</b>   | <b>9,169</b>                               | <b>954</b>                     | <b>1,197</b>  | <b>279</b>                  | <b>693</b>     | <b>(688)</b>                              | <b>11,604</b>  |
| Net insurance claims <sup>1</sup>   | (124)                                      |                                |   |                             |                |   | (124)          |
| <b>Net operating income before loan<br/>impairment charges and other credit<br/>risk provisions</b> | <b>9,045</b>                               | <b>954</b>                     | <b>1,197</b>  | <b>279</b>                  | <b>693</b>     | <b>(688)</b>                              | <b>11,480</b>  |
| Loan impairment (charges)/recoveries<br>and other credit risk provisions                            | (3,774)                                    | (46)                           | 12  | (12)                        |                |   | (3,820)        |
| <b>Net operating income</b>   | <b>5,271</b>                               | <b>908</b>                     | <b>1,209</b>  | <b>267</b>                  | <b>693</b>     | <b>(688)</b>                              | <b>7,660</b>   |
| Total operating expenses  | (3,783)                                    | (443)                          | (771)   | (207)                       | (719)          | 688                                       | (5,235)        |
| <b>Operating profit/(loss)</b>  | <b>1,488</b>                               | <b>465</b>                     | <b>438</b>  | <b>60</b>                   | <b>(26)</b>    |   | <b>2,425</b>   |
| Share of profit/(loss) in associates and<br>joint ventures  |  | 12                             | (2)   |                             |                |   | 10             |
| <b>Profit/(loss) before tax</b>   | <b>1,488</b>                               | <b>477</b>                     | <b>436</b>  | <b>60</b>                   | <b>(26)</b>    |   | <b>2,435</b>   |

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|                                   | %    | %    | %    | %    | %     | %    |
|-----------------------------------|------|------|------|------|-------|------|
| Share of HSBC's profit before tax | 10.5 | 3.4  | 3.1  | 0.4  | (0.2) | 17.2 |
| Cost efficiency ratio             | 41.8 | 46.4 | 64.4 | 74.2 | 103.8 | 45.6 |

**Balance sheet data<sup>2</sup>**

|                                       | US\$m   | US\$m  | US\$m   | US\$m  | US\$m | US\$m   |
|---------------------------------------|---------|--------|---------|--------|-------|---------|
| Loans and advances to customers (net) | 219,735 | 34,831 | 21,462  | 5,267  |       | 281,295 |
| Total assets                          | 246,117 | 41,227 | 223,435 | 6,386  | 2,528 | 519,693 |
| Customer accounts                     | 58,724  | 33,513 | 27,661  | 14,392 | 107   | 134,397 |

|  |  |  |         |  |  |  |
|--|--|--|---------|--|--|--|
| Loans and advances to banks (net) <sup>3</sup>   |  |  | 16,289  |  |  |  |
| Trading assets, financial instruments<br>designated at fair value, and financial<br>investments <sup>3</sup> |  |  | 142,088 |  |  |  |
| Deposits by banks <sup>3</sup>   |  |  | 10,927  |  |  |  |

*For footnotes, see page 62.*



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Half-year to 30 June 2006<sup>4</sup>

|   | Personal<br>Financial<br>Services<br>US\$m | Commercial<br>Banking<br>US\$m | Corporate,<br>Investment<br>Banking &<br>Markets<br>US\$m | Private<br>Banking<br>US\$m | Other<br>US\$m | Inter-<br>segment<br>elimination<br>US\$m | Total<br>US\$m |
|---|--|--------------------------------|---|-----------------------------|----------------|---|----------------|
| <b>North America</b>  |  |                                |   |                             |                |   |                |
| Net interest income/(expense)   | 6,467                                      | 639                            | 162   | 102                         | (31)           | (343)                                     | 6,996          |
| Net fee income/(expense)  | 1,823                                      | 150                            | 322   | 119                         | (102)          |   | 2,312          |
| Trading income/(expense) excluding net<br>interest income   | 117  | 4                              | 406   | 6                           | (66)           |   | 467            |
| Net interest income/(expense) on<br>trading activities  | 98   |                                | 53  |                             | (2)            | 343                                       | 492            |
| Net trading income/(expense)  | 215  | 4                              | 459   | 6                           | (68)           | 343                                       | 959            |
| Net income/(expense) from financial<br>instruments designated at fair value                         |  |                                | 35  |                             | (11)           |   | 24             |
| Gains less losses from financial<br>investments   | 20   | 9                              | 9   | 3                           | (1)            |   | 40             |
| Dividend income   | 5  |                                | 33  |                             | 1              |   | 39             |
| Net earned insurance premiums   | 237  |                                |   |                             | 1              |   | 238            |
| Other operating income  | 134  | 50                             | 83  | 11                          | 702            | (615)                                     | 365            |
| <b>Total operating income</b>   | <b>8,901</b>                               | <b>852</b>                     | <b>1,103</b>  | <b>241</b>                  | <b>491</b>     | <b>(615)</b>                              | <b>10,973</b>  |
| Net insurance claims <sup>1</sup>   | (118)                                      |                                |   |                             | 1              |   | (117)          |
| <b>Net operating income before loan<br/>impairment charges and other credit risk<br/>provisions</b> | <b>8,783</b>                               | <b>852</b>                     | <b>1,103</b>  | <b>241</b>                  | <b>492</b>     | <b>(615)</b>                              | <b>10,856</b>  |
| Loan impairment (charges)/recoveries<br>and other credit risk provisions                            | (2,117)                                    | (31)                           | 6   | (30)                        |                |   | (2,172)        |
| <b>Net operating income</b>   | <b>6,666</b>                               | <b>821</b>                     | <b>1,109</b>  | <b>211</b>                  | <b>492</b>     | <b>(615)</b>                              | <b>8,684</b>   |
| <b>Total operating expenses</b>   | <b>(3,649)</b>                             | <b>(387)</b>                   | <b>(761)</b>  | <b>(173)</b>                | <b>(619)</b>   | <b>615</b>                                | <b>(4,974)</b> |
| <b>Operating profit/(loss)</b>  | <b>3,017</b>                               | <b>434</b>                     | <b>348</b>  | <b>38</b>                   | <b>(127)</b>   |   | <b>3,710</b>   |
| Share of profit in associates and joint<br>ventures   |  | 30                             | 1   |                             |                |   | 31             |
| <b>Profit/(loss) before tax</b>   | <b>3,017</b>                               | <b>464</b>                     | <b>349</b>  | <b>38</b>                   | <b>(127)</b>   |   | <b>3,741</b>   |
|   | %  | %                              | %   | %                           | %              |   | %              |
| Share of HSBC's profit before tax   | 24.1                                       | 3.7                            | 2.8   | 0.3                         | (1.0)          |   | 29.9           |
| Cost efficiency ratio   | 41.5                                       | 45.4                           | 69.0  | 71.8                        | 125.8          |   | 45.8           |
| <b>Balance sheet data<sup>2</sup></b>   |  |                                |   |                             |                |   |                |
|   | US\$m                                      | US\$m                          | US\$m   | US\$m                       | US\$m          |   | US\$m          |
| Loans and advances to customers (net)   | 218,291                                    | 31,842                         | 13,769  | 4,968                       |                |   | 268,870        |
| Total assets  | 248,176                                    | 40,218                         | 199,739   | 5,836                       | 1,926          |   | 495,895        |

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|  |        |        |         |        |    |         |
|--|--------|--------|---------|--------|----|---------|
| Customer accounts  | 50,612 | 29,404 | 31,475  | 11,918 | 97 | 123,506 |
| Loans and advances to banks (net) <sup>3</sup>   |        |        | 14,753  |        |    |         |
| Trading assets, financial instruments<br>designated at fair value, and financial<br>investments <sup>3</sup> |        |        | 132,744 |        |    |         |
| Deposits by banks <sup>3</sup>   |        |        | 8,315   |        |    |         |

*For footnotes, see page 62.*

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**Business Review** (continued)

Profit/(loss) before tax and balance sheet data by customer group and global business (continued)

|   | Half-year to 31 December 2006              |                                |   |                             |                |   |                |
|---|--|--------------------------------|---|-----------------------------|----------------|---|----------------|
|   | Personal<br>Financial<br>Services<br>US\$m | Commercial<br>Banking<br>US\$m | Corporate,<br>Investment<br>Banking &<br>Markets<br>US\$m | Private<br>Banking<br>US\$m | Other<br>US\$m | Inter-<br>segment<br>elimination<br>US\$m | Total<br>US\$m |
| <b>North America</b>  |  |                                |   |                             |                |   |                |
| Net interest income/(expense)                                   | 6,497                                      | 723                            | 104   | 110                         | (21)           | (141)                                     | 7,272          |
| Net fee income/(expense)  | 1,852                                      | 179                            | 334   | 121                         | (32)           |   | 2,454          |
| Trading income/(expense) excluding net interest income          | (51)                                       | 9                              | 340   | 6                           | (154)          |   | 150            |
| Net interest income/(expense) on trading activities             | 110  |                                | 19  |                             | (21)           | 141                                       | 249            |
| Net trading income/(expense)                                    | 59   | 9                              | 359   | 6                           | (175)          | 141                                       | 399            |
| Net expense from financial instruments designated at fair value |  |                                | (46)  |                             | (41)           |   | (87)           |
| Gains less losses from financial investments                    | (6)  | 10                             | 3   | 6                           | 5              |   | 18             |
| Dividend income   | 18   | 1                              | 28  |                             | (1)            |   | 46             |
| Net earned insurance premiums                                   | 255  |                                |   |                             | (1)            |   | 254            |
| Other operating income  | 136  | 37                             | 186   | 20                          | 834            | (656)                                     | 557            |
| <b>Total operating income</b>                                   | <b>8,811</b>                               | <b>959</b>                     | <b>968</b>  | <b>263</b>                  | <b>568</b>     | <b>(656)</b>                              | <b>10,913</b>  |
| Net insurance claims <sup>1</sup>                               | (141)                                      |                                |   |                             | (1)            |   | (142)          |
| <b>Net operating income<sup>5</sup></b>                         | <b>8,670</b>                               | <b>959</b>                     | <b>968</b>  | <b>263</b>                  | <b>567</b>     | <b>(656)</b>                              | <b>10,771</b>  |
| Loan impairment charges and other credit risk provisions        | (4,566)                                    | (43)                           | (9)   | (5)                         | (1)            |   | (4,624)        |
| <b>Net operating income</b>                                     | <b>4,104</b>                               | <b>916</b>                     | <b>959</b>  | <b>258</b>                  | <b>566</b>     | <b>(656)</b>                              | <b>6,147</b>   |
| <b>Total operating expenses</b>                                 | <b>(3,730)</b>                             | <b>(427)</b>                   | <b>(880)</b>  | <b>(182)</b>                | <b>(656)</b>   | <b>656</b>                                | <b>(5,219)</b> |
| <b>Operating profit/(loss)</b>                                  | <b>374</b>                                 | <b>489</b>                     | <b>79</b>   | <b>76</b>                   | <b>(90)</b>    |   | <b>928</b>     |
| Share of profit/(loss) in associates and joint ventures         |  | 4                              | (5)   |                             |                |   | (1)            |
| <b>Profit/(loss) before tax</b>                                 | <b>374</b>                                 | <b>493</b>                     | <b>74</b>   | <b>76</b>                   | <b>(90)</b>    |   | <b>927</b>     |
|   | %  | %                              | %   | %                           | %              |   | %              |
| Share of HSBC's profit before tax                               | 3.9  | 5.2                            | 0.8   | 0.8                         | (1.0)          |   | 9.7            |
| Cost efficiency ratio   | 43.0                                       | 44.5                           | 90.9  | 69.2                        | 115.7          |   | 48.5           |

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Balance sheet data<sup>2</sup>

|  | US\$m   | US\$m  | US\$m   | US\$m  | US\$m | US\$m   |
|--|---------|--------|---------|--------|-------|---------|
| Loans and advances to customers (net)  | 220,517 | 34,651 | 17,215  | 5,604  |       | 277,987 |
| Total assets   | 250,985 | 43,012 | 208,958 | 6,558  | 1,677 | 511,190 |
| Customer accounts  | 54,099  | 31,066 | 23,711  | 11,938 | 108   | 120,922 |
| Loans and advances to banks (net) <sup>3</sup>   |         |        | 15,862  |        |       |         |
| Trading assets, financial instruments designated at fair value, and financial investments <sup>3</sup> |         |        | 136,141 |        |       |         |
| Deposits by banks <sup>3</sup>   |         |        | 9,664   |        |       |         |

1 Net insurance claims incurred and movement in policyholders' liabilities.

2 Third party only.

3 These assets and liabilities were significant to Corporate, Investment Banking and Markets.

4 In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

5 Net operating income before loan impairment charges and other credit risk provisions.

[Back to Contents](#)**Latin America**

Profit/(loss) before tax by country within customer groups and global businesses

|                                  | Personal<br>Financial<br>Services<br>US\$m | Commercial<br>Banking<br>US\$m | Corporate,<br>Investment<br>Banking &<br>Markets<br>US\$m | Private<br>Banking<br>US\$m | Other<br>US\$m | Total<br>US\$m |
|----------------------------------|--|--------------------------------|---|-----------------------------|----------------|----------------|
| <b>Half-year to 30 June 2007</b> |  |                                |   |                             |                |                |
| Mexico                           | 251  | 169                            | 50  | 5                           |                | 475            |
| Brazil                           | 101  | 116                            | 141   | 4                           | (2)            | 360            |
| Argentina                        | 10   | 33                             | 49  |                             | 3              | 95             |
| Other                            | 26   | 34                             | 13  | 1                           | (4)            | 70             |
|                                  | <u>388</u>                                 | <u>352</u>                     | <u>253</u>  | <u>10</u>                   | <u>(3)</u>     | <u>1,000</u>   |

Half-year to 30 June 2006<sup>1</sup>

|           |            |            |            |          |            |            |
|-----------|------------|------------|------------|----------|------------|------------|
| Mexico    | 284        | 127        | 105        | (1)      |            | 515        |
| Brazil    | 42         | 82         | 124        | 3        |            | 251        |
| Argentina | 23         | 21         | 37         |          | 2          | 83         |
| Other     | 5          | 7          | 11         | 1        | (8)        | 16         |
|           | <u>354</u> | <u>237</u> | <u>277</u> | <u>3</u> | <u>(6)</u> | <u>865</u> |

## Half-year to 31 December 2006

|           |            |            |            |           |          |            |
|-----------|------------|------------|------------|-----------|----------|------------|
| Mexico    | 344        | 70         | 72         | 8         |          | 494        |
| Brazil    | 79         | 103        | 94         | 3         | (4)      | 275        |
| Argentina | 12         | 30         | 31         |           | 1        | 74         |
| Other     | 11         | 11         | 1          |           | 4        | 27         |
|           | <u>446</u> | <u>214</u> | <u>198</u> | <u>11</u> | <u>1</u> | <u>870</u> |

## Loans and advances to customers (net) by country

|           | Half-year to             |                                       |                                 |
|-----------|--------------------------|---------------------------------------|---------------------------------|
|           | 30 June<br>2007<br>US\$m | 30 June<br>2006 <sup>1</sup><br>US\$m | 31<br>December<br>2006<br>US\$m |
| Mexico    | 16,063                   | 12,043                                | 14,294                          |
| Brazil    | 14,104                   | 9,635                                 | 11,469                          |
| Argentina | 2,026                    | 1,666                                 | 1,912                           |
| Other     | 8,413                    | 1,603                                 | 8,116                           |
|           | <u>40,606</u>            | <u>24,947</u>                         | <u>35,791</u>                   |

Customer accounts by country

|           | Half-year to                      |                                       |                                 |
|-----------|-----------------------------------|---------------------------------------|---------------------------------|
|           | <b>30 June<br/>2007<br/>US\$m</b> | 30 June<br>2006 <sup>1</sup><br>US\$m | 31<br>December<br>2006<br>US\$m |
| Mexico    | <b>19,916</b>                     | 18,688                                | 19,775                          |
| Brazil    | <b>23,660</b>                     | 17,232                                | 19,946                          |
| Argentina | <b>2,659</b>                      | 2,103                                 | 2,470                           |
| Other     | <b>9,014</b>                      | 2,054                                 | 8,670                           |
|           | <b>55,249</b>                     | 40,077                                | 50,861                          |

1 In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

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**Business Review** (continued)

Profit before tax

|  | Half-year to             |                                       |                                 |
|--|--------------------------|---------------------------------------|---------------------------------|
|  | 30 June<br>2007<br>US\$m | 30 June<br>2006 <sup>1</sup><br>US\$m | 31<br>December<br>2006<br>US\$m |
| <b>Latin America</b>   |                          |                                       |                                 |
| Net interest income  | 2,534                    | 2,004                                 | 2,193                           |
| Net fee income   | 998                      | 770                                   | 860                             |
| Net trading income   | 285                      | 258                                   | 279                             |
| Net income from financial instruments designated at fair value   | 157                      | 106                                   | 131                             |
| Gains less losses from financial investments   | 98                       | 38                                    | 46                              |
| Dividend income  | 6                        | 3                                     | 3                               |
| Net earned insurance premiums  | 731                      | 522                                   | 554                             |
| Other operating income   | 153                      | 41                                    | 50                              |
| <b>Total operating income</b>  | <b>4,962</b>             | <b>3,742</b>                          | <b>4,116</b>                    |
| Net insurance claims incurred and movement in policyholders' liabilities                               | (676)                    | (489)                                 | (534)                           |
| <b>Net operating income before loan impairment charges and other credit risk provisions</b>            | <b>4,286</b>             | <b>3,253</b>                          | <b>3,582</b>                    |
| Loan impairment charges and other credit risk provisions   | (775)                    | (442)                                 | (496)                           |
| <b>Net operating income</b>  | <b>3,511</b>             | <b>2,811</b>                          | <b>3,086</b>                    |
| Total operating expenses   | (2,516)                  | (1,946)                               | (2,220)                         |
| <b>Operating profit</b>  | <b>995</b>               | <b>865</b>                            | <b>866</b>                      |
| Share of profit in associates and joint ventures   | 5                        |                                       | 4                               |
| <b>Profit before tax</b>   | <b>1,000</b>             | <b>865</b>                            | <b>870</b>                      |
|  | %                        | %                                     | %                               |
| Share of HSBC's profit before tax  | 7.1                      | 6.9                                   | 9.1                             |
| Cost efficiency ratio  | 58.7                     | 59.8                                  | 62.0                            |
| Period-end staff numbers (full-time equivalent)  | 66,875                   | 55,241                                | 64,900                          |
| <b>Balance sheet data<sup>2</sup></b>  |                          |                                       |                                 |
|  | US\$m                    | US\$m                                 | US\$m                           |
| Loans and advances to customers (net)  | 40,606                   | 24,947                                | 35,791                          |
| Loans and advances to banks (net)  | 13,345                   | 9,418                                 | 12,634                          |
| Trading assets, financial instruments designated at fair value, and financial investments <sup>2</sup> | 22,107                   | 17,171                                | 20,497                          |
| Total assets   | 88,925                   | 58,997                                | 80,771                          |

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|                   |        |        |        |
|-------------------|--------|--------|--------|
| Deposits by banks | 4,727  | 2,335  | 5,267  |
| Customer accounts | 55,249 | 40,077 | 50,861 |

- 1 *In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.*
- 2 *Third party only.*

### Economic briefing

Economic activity slowed in **Mexico** during the first quarter of 2007. Annualised GDP growth fell to 2.6 per cent year-on-year, down from an average rate of 4.8 per cent in 2006, mainly from a sharp slowdown in industrial production caused by a fall in US demand for Mexican manufactured goods, especially motor vehicles. Construction activity also reduced and the unemployment rate rose slightly, averaging 3.8 per cent in January-May compared with 3.4 per cent in the same period in 2006. Subsequently, there were signs of a recovery, with industrial surveys and production improving and non-

oil exports rising to 10.8 per cent year-on-year in April, the first double-digit increase since last October. Headline inflation was favoured by abnormally low readings for fruit and vegetable prices during May 2007, when the CPI fell by 0.5 per cent, the sharpest decline recorded in any month since the index began, but inflation throughout the first half of 2007 none the less remained at approximately 4 per cent, above the 3 per cent target. With many potential price increases expected in key variables such as energy, grain and corn, the Bank of Mexico raised interest rates by 25 basis points to 7.25 per cent in April 2007 after eleven months with no change.



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In **Brazil**, economic activity accelerated in the first half of 2007, with GDP growing by 4.3 per cent year-on-year in the first quarter and industrial production rising by 4.4 per cent year-on-year in the five months ended May 2007. Growth continued to be driven by domestic demand, with private consumption and capital spending rising by 6.0 per cent and 7.2 per cent respectively. The unemployment rate of 9.8 per cent was slightly lower than for the same period in 2006, and consumer price inflation was relatively low at 3.2 per cent year-on-year. As a result of the benign conditions, the Central Bank of Brazil continued to ease monetary policy. Overnight rates fell to 12 per cent in June 2007, down from 13.25 per cent at the end of 2006 and 18 per cent in June 2006. Although the exchange rate appreciated, the trade balance continued to post a substantial surplus of US\$20.6 billion in the first half of 2007.

**Argentina**'s growth slipped to 8 per cent year-on-year in the first quarter of 2007 from an average of 8.5 per cent in 2006. Investment growth slowed, largely reflecting a fall in construction activity. Private spending growth in the first quarter rose slightly to 8.2 per cent, driven by strong job creation, higher real wages and an increase in public spending in an election year. Personal loan demand remained robust, though current growth rates (40 per cent year-on-year) are not expected to be sustained during the rest of 2007. Interest rates stayed low as a consequence of the authorities' monetary and exchange rate policies, the main objective of which was to prevent the peso from strengthening. Inflation averaged 9.2 per cent in the first half of 2007, though methodological changes mean that this figure is not comparable to the average level of 11.1 per cent reported in 2006. Under the old methodology, inflation would have increased in 2007.

### Review of business performance

HSBC's operations in Latin America reported a pre-tax profit of US\$1,000 million compared with US\$865 million in the first half of 2006, an increase of 16 per cent. During 2006, HSBC acquired Grupo Banistmo in Central America and Banca Nazionale del Lavoro SpA ( Banca Nazionale ) in Argentina, complementing existing businesses and expanding HSBC's geographical presence by 5 new countries. On an underlying basis, pre-tax profits rose by 7 per cent. Commercial Banking reported pre-tax profits which were 49 per cent higher than in the first half of 2006, with notable contributions made by the businesses in Mexico and Brazil, where underlying pre-tax profits rose by 35 per cent and 32 per cent, respectively. Increases in the region were driven by

asset growth and increased fees. An additional four months of profits from Banca Nazionale increased profits in Argentina in both Commercial Banking and Personal Financial Services. In the latter, underlying profit before tax rose compared with the first half of 2006 as the benefit of balance sheet growth and higher fee income was partially offset by the higher costs and loan impairment charges experienced in Mexico. Profit before tax in CIBM decreased, largely as a result of lower balance sheet management income in Mexico.

The following commentary is on an underlying basis.

**Personal Financial Services** reported a pre-tax profit of US\$388 million, a 2 per cent increase on the first half of 2006. Revenues rose, reflecting balance sheet growth, improved fees and an additional four months of Banca Nazionale revenues. A refinement in the income recognition methodology in respect of long-term insurance contracts in Mexico resulted in a one-off revenue increment of US\$69 million. Expansion-driven cost growth, together with a related significant rise in loan impairment charges in Mexico, partly mitigated the benefit of increased revenues. The cost efficiency ratio improved 2.6 percentage points as revenues grew faster than costs.

Net interest income rose by 13 per cent to US\$1,821 million from asset and liability growth, partly offset by lower deposit spreads.

In Mexico, net interest income rose by 22 per cent from balance sheet growth and improved asset spreads. Average deposit balances rose by 9 per cent. The 'Tu Cuenta' bundled product was the key factor behind this growth as balances reached US\$1.1 billion at 30 June 2007. HSBC also introduced 'Cuenta Chicos HSBC' in a joint venture with the Disney Corporation aimed at the fast developing youth market. The Premier segment performed well, and increased cross-sales led to a rise in the number of products held per customer. Premier deposit balances at 30 June 2007 were US\$6.0 billion, helped by an expansion in customer numbers.

Continued investment in HSBC Mexico's credit cards business resulted in strong sales volumes and average balance growth of 124 per cent. A combination of new customer acquisitions, an effective marketing promotion and portfolio management campaigns to increase usage and improve customer retention, led to higher volumes. These factors, along with attractive balance transfer terms and special introductory rates, helped HSBC improve its market share by 340 basis points. The



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HSBC HOLDINGS PLC

## Business Review (continued)

number of cards in circulation grew by 50 per cent to reach 2.2 million, driven by increased cross-sales and the introduction of a new platinum card.

The mortgage market in Mexico was highly competitive, as demand for housing remained strong. Average mortgage balances rose by 23 per cent, supported by the continued success of the Mortgage Express Approval product and improved operational efficiencies. A greater level of sales activity following the introduction of a mobile sales force in the latter part of 2006 also contributed to the increase. Mortgage spreads narrowed in the competitive market. Furthermore, during the first quarter of 2007, a US\$227 million residential mortgage portfolio was securitised which, at the time, was the largest transaction of its kind undertaken in Latin America.

There was a significant rise in self-employed and payroll lending balances, fuelled by favourable economic conditions. Average self-employed loan balances rose by 131 per cent, aided by the mobile sales force that reduced time to market, together with increased cross-sales and improved client coverage. Average payroll loan balances grew by 65 per cent, reflecting HSBC's extensive and well positioned ATM network.

In Brazil, net interest income of US\$931 million was 6 per cent higher. A stable inflation rate, the positive economic outlook and falling interest rates led to robust demand for credit. Average lending balances grew by 26 per cent, primarily driven by growth in vehicle financing, pension and payroll loans.

Average motor vehicle balances rose by 45 per cent, and HSBC's market share improved as the Group strengthened its relationships with dealers, improved its systems and reduced processing times. There was an 83 per cent rise in average balances in the combined pension and payroll loan portfolios, driven by the effects of strong customer demand, acquisitions of payroll accounts and a rise in the average loan size per customer.

A rise in borrowing limits to customers with good credit records led to a 26 per cent increase in average instalment loan balances. Average credit card balances rose by 19 per cent, following steps taken to improve retention, activation and utilisation which, when combined with a new private label and co-branded card launched in conjunction with Visa to capture business from new merchants, led to an 18 per cent increase in the number of cards in force.

In Argentina, net interest income grew by 34 per cent from an extra four months of Banca Nazionale revenues, together with strong asset and deposit growth, partly offset by reduced deposit spreads. Greater cross-sales activity led to balance growth in cards, vehicle finance and other personal lending. Average deposit balances rose by 24 per cent with the resulting income benefit partly offset by reduced spreads.

Net fee income was 21 per cent higher, principally driven by Mexico and Brazil.

In Mexico, fee income rose by 32 per cent, largely due to higher credit card, Tu Cuenta and ATM fees. An increase in card fees reflected HSBC's strategy of investing in this business, and the consequent growth in both customer numbers and the number of cards in circulation. Fees from the Tu Cuenta packaged product rose strongly, following sales of nearly 380,000 new accounts. ATM fees grew from increased transaction volumes, as HSBC continued to expand its already well-positioned network with the addition of 249 new machines.

In Brazil, fee income rose by 4 per cent, primarily due to higher current account fees and improved credit fees. In Argentina, growth reflected increased transactional activity, higher card and vehicle finance balances, and an extra four months of Banca Nazionale revenues.

The insurance operations across the region continued to perform well, as HSBC invested in new products, expanded distribution channels, increased cross-sales and implemented its bancassurance model across Central America. The results also benefited from a refinement in the income recognition methodology in respect of long-term insurance contracts in Mexico, which resulted in a one-off revenue increment of US\$69 million.

In Mexico, greater cross-sales activity in the branch network led to higher premiums from life insurance and motor vehicle finance products. In Brazil, pension-related premiums rose following marketing campaigns, and the introduction of a life insurance product offered to customers applying for instalment loans proved successful. In Argentina, the increase reflected higher motor and home insurance, life and annuity

premiums.

Loan impairment charges rose by 55 per cent, largely following growth in credit expansion in fast growing markets, particularly in Mexico.

In Mexico, significant growth in credit card and self-employed lending balances, areas in which HSBC traditionally had a low market presence, led to an increase in loan impairment charges. Delinquency rates rose during the period as the loan book grew. Loan underwriting criteria and collections strategies are regularly reviewed to maintain the quality of the

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portfolio. Loan impairment charges were also affected by changes made to the consumer portfolio credit models to more accurately represent actual credit behaviour in the underlying portfolios.

Loan impairment charges in Brazil declined in response to tightening of credit approval policies, increased collections activity and growth in secured lending such as vehicle and payroll loans, and consequently, impaired loans as a proportion of total assets declined. In Argentina, growth in lending and the inclusion of the Banca Nazionale portfolio resulted in higher loan impairment charges.

Operating expenses increased by 16 per cent.

In Mexico, the rise was primarily driven by a combination of higher staff numbers and marketing costs incurred to support business expansion. Staff costs grew, following the recruitment of approximately 1,600 additional employees and a higher fiscal base for statutory profit sharing, while marketing costs rose from Tu Cuenta and credit card campaigns. Investments made to the branch and the ATM infrastructure led to higher premises and equipment costs. Despite this growth in expenses, the cost efficiency ratio improved by 6.1 percentage points.

In Brazil, expenses grew by 11 per cent. Staff costs increased from one-off expenses incurred to improve future operational efficiencies as HSBC continued to position itself for future growth, and union-agreed pay rises took effect. Non-staff expenses increased as a result of investments in system improvements designed to reduce processing times for vehicle loans, and to further develop the direct sales channels from which 20 per cent of the total Personal Financial Services network business was generated. Marketing and transactional taxes rose in light of the improved revenues, while various payroll account acquisitions and the consequent increase in account holders led to higher amortisation costs.

In Argentina, the 65 per cent rise in expenses was primarily due to the inclusion of an additional four months of Banca Nazionale costs. Staff costs grew due to pay rises and additional headcount to support higher revenues. Marketing and advertising costs rose from various campaigns and the rebranding of Banca Nazionale to HSBC. Investments enabling customers to conduct a wider range of transactions online led to higher IT costs.

**Commercial Banking** reported pre-tax profits of US\$352 million, an increase of 34 per cent over the first half of 2006. Revenues rose from asset growth, increased fees and an additional four months of

Banca Nazionale profits following its acquisition in May 2006. The cost efficiency ratio improved by 110 basis points. Loan impairment charges also fell following reduced charges in Mexico.

Net interest income rose by 16 per cent, driven by asset growth and improved lending spreads, partly offset by declines in liability balances in Mexico.

In Mexico, net interest income rose by 18 per cent to US\$235 million, reflecting strong asset growth with higher real estate balances, and a rise in lending balances from small and medium sized business clients.

Average lending balances rose by 36 per cent, primarily reflecting robust demand in the fast growing real estate and residential construction sectors. HSBC improved its capacity to meet the needs of clients involved in residential and tourist construction, improving its presence in this market. The small and medium-sized business portfolios continued to perform well, with balance growth of 148 per cent accompanied by a 24 per cent rise in customer numbers. The International Banking Centre that was opened in Mexico during the latter part of 2006 now supports Central America and Colombia in order to develop greater levels of cross-border business activity for regional and global Commercial Banking customers.

In Brazil, net interest income increased by 11 per cent, mostly due to increased lending to corporate and medium-sized businesses with higher trade balances, and robust demand for receivables-backed loans and agricultural loans. Increased focus on promoting government loans, where HSBC acted as the intermediary, led to growth in loan balances of 101 per cent. In the small and micro business segments, changes to borrowing limits for customers with good credit records led to higher balances. The giro facil product performed well, helped by marketing campaigns and the recent introduction of ATM applications. Attractive rates offered in a highly competitive market also contributed to asset growth, but spreads narrowed.

Strong asset and liability growth in Argentina and incremental Banca Nazionale revenues led to an 85 per cent increase in net interest income. Average loan balances rose by 29 per cent from growth in customer numbers, new products and increased marketing. There was particularly strong growth in the leasing and agribusiness portfolios. A greater emphasis on promoting receivable financing in line with HSBC's global strategy led to an 80 per cent rise in this portfolio. Asset and deposit spreads widened which, combined with deposit growth, contributed further to the increase.



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HSBC HOLDINGS PLC

## Business Review (continued)

Net fee income was 20 per cent higher, primarily driven by robust growth across the region.

In Mexico, fee income grew by 21 per cent. Higher payment and cash management revenues reflected increased customer numbers and greater transaction volumes. New merchant relationship agreements and a rise in the number of point of service terminals led to higher card acquiring fees. Fees from the award winning Estimulo product increased by 109 per cent, attributable to higher sales volumes as nearly 4,000 new packages were sold since 30 June 2006. An increased focus on growing structured debt market revenues, and greater cross-sales activity, led to higher trust fees. HSBC's market share in trade services grew by nearly 4 percentage points as the Group made its geographical presence and enhanced product capabilities felt.

In Brazil, fees rose as re-pricing initiatives triggered higher current account, payment and cash management fees. The latter also benefited from increased transactional activity. Insurance, credit and funds under management fees were also higher. Fee income in Argentina grew, primarily due to incremental Banca Nazionale revenues, increased transaction volumes and re-pricing initiatives.

Loan impairment charges fell by 16 per cent to US\$74 million, due to releases in Mexico.

In Mexico, loan impairment charges fell as changes were made to credit models for the commercial loan portfolio to more accurately represent most recent credit behaviour in the underlying portfolios. This was partly offset by higher charges related to the fast growing small and medium business loan books. Loan underwriting criteria and collections strategies are regularly reviewed to maintain the quality of the portfolio.

Loan impairment charges rose by 8 per cent in Brazil from higher charges required in the corporate segment, partly offset by reductions in both the mid-market and the small and micro business segments. In Argentina, higher charges reflected the effect of the Banca Nazionale acquisition.

Operating expenses of US\$523 million were 18 per cent higher from continued investments made across the region in developing the Commercial Banking platform.

In Mexico, operating expenses increased by 18 per cent. Staff costs rose, reflecting additional headcount to support business growth and a higher fiscal base for statutory profit sharing. Non-staff costs also increased, attributable to a rise in branch transaction costs from greater business volumes and higher IT costs.

Operating expenses in Brazil grew by 13 per cent. Staff costs grew following the introduction of union-agreed pay rises, and from an increased focus on improving efficiencies in the small and micro business segments, which resulted in one-off costs being incurred. Branch expenses and transactional taxes also increased, reflecting revenue growth. The increase in Argentina reflected union-agreed pay rises, higher marketing and IT costs and an additional four months of Banca Nazionale costs.

**Corporate, Investment Banking and Markets** in Latin America reported a pre-tax profit of US\$253 million, which represented 7 per cent of the global business's pre-tax profits, and a decrease of 12 per cent compared with the first half of 2006. In Mexico, pre-tax profits declined by 53 per cent, largely due to lower income from balance sheet management. This was partly offset by pre-tax profit increases reported in Argentina and Brazil, although HSBC's results in Argentina included an additional four months contribution from Banca Nazionale. The cost efficiency ratio deteriorated by 5.8 percentage points.

A decrease in net interest income was primarily driven by the adverse impact of a flat yield curve on balance sheet management activity in Mexico. By contrast, Brazil and Argentina benefited from lower funding costs against the background of a decreasing interest rate environment. An 11 per cent rise in payments and cash management income across the region was due to an increase in transaction volumes and the acquisition of new clients.

Net fee income increased by 15 per cent to US\$109 million, mostly driven by higher fees in Brazil. Securities services revenue rose as new business volumes and strong local equity markets drove a 56 per cent increase in assets under custody. Investment banking fees also increased.

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Income from trading activities was 8 per cent higher than in the first half of 2006. Brazil reported a rise in revenues, mainly due to a successful strategy to provide a wider range of products to HSBC's customers, while Panama recorded an increase resulting from strong customer volumes. In Mexico, trading revenues continued to be driven by strong gains in foreign exchange, partly offset by lower interest rate derivatives income and a decline in credit and rates revenue as opportunities were constrained by a flat yield curve.

Gains less losses from financial investments increased by 57 per cent, largely due to gains on the disposal of floating rate bonds in Argentina and securities in Brazil and in Mexico.



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Loan impairment releases decreased due to the non-recurrence of a large release in Mexico in 2006.

Operating expenses rose by 21 per cent to US\$211 million, in part due to the inclusion of costs related to Banca Nazionale in Argentina. In Mexico, increased costs were largely due to a higher fiscal base for profit sharing. Higher costs in Brazil reflected investments in technology to enhance the corporate lending capabilities.

Increased operational costs resulted from product and distribution expansion initiatives implemented in recent periods, reflecting HSBC's continued investment in emerging markets.

**Private Banking** continued to make good progress in the region, with pre-tax profits of US\$10 million being more than three times those reported in the first half of 2006. The cost efficiency ratio improved by 17.8 percentage points to 65.5 per cent.

Net interest income grew by 33 per cent, reaching US\$8 million, driven by balance sheet growth as the business expanded in the region.

Demand from clients for broking in Mexico and for investment in funds in Brazil resulted in a doubling of net fee income to US\$16 million.

Client assets of US\$8 billion were 31 per cent higher than at 31 December 2006, following growth in the onshore client base and demand for investment in funds by clients, with over US\$600 million of net new money attracted in the first six months of the year.

As the onshore Private Banking business in Latin America expanded, operating expenses increased by 27 per cent to support the growth. This was 34 percentage points lower than the rate of growth of income, which resulted in the improvement in the cost efficiency ratio.

Amounts reported within **Other** were broadly in line with the first half of 2006.

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HSBC HOLDINGS PLC

**Business Review** (continued)

Profit/(loss) before tax and balance sheet data by customer group and global business

Half-year to 30 June 2007

|   | Personal<br>Financial<br>Services<br>US\$m | Commercial<br>Banking<br>US\$m | Corporate,<br>Investment<br>Banking &<br>Markets<br>US\$m | Private<br>Banking<br>US\$m | Other<br>US\$m | Inter-<br>segment<br>elimination<br>US\$m | Total<br>US\$m |
|---|--|--------------------------------|---|-----------------------------|----------------|---|----------------|
| <b>Latin America</b>  |  |                                |   |                             |                |   |                |
| Net interest income   | 1,821                                      | 656                            | 181   | 8                           | 1              | (133)                                     | 2,534          |
| Net fee income  | 636  | 234                            | 109   | 16                          | 3              |   | 998            |
| Trading income/(expense) excluding<br>net interest income   | 32   | 17                             | 83  | 1                           | (1)            |   | 132            |
| Net interest income on trading<br>activities  | 6  | 1                              | 13  |                             |                | 133                                       | 153            |
| Net trading income/(expense)  | 38   | 18                             | 96  | 1                           | (1)            | 133                                       | 285            |
| Net income from financial<br>instruments designated at fair value                                   | 153  |                                | 4   |                             |                |   | 157            |
| Gains less losses from financial<br>investments   | 30   | 13                             | 55  |                             |                |   | 98             |
| Dividend income   | 4  | 1                              | 1   |                             |                |   | 6              |
| Net earned insurance premiums   | 658  | 32                             | 41  |                             |                |   | 731            |
| Other operating income  | 134  | 12                             | 8   | 4                           | 8              | (13)                                      | 153            |
| <b>Total operating income</b>   | <b>3,474</b>                               | <b>966</b>                     | <b>495</b>  | <b>29</b>                   | <b>11</b>      | <b>(13)</b>                               | <b>4,962</b>   |
| Net insurance claims <sup>1</sup>   | (626)                                      | (17)                           | (33)  |                             |                |   | (676)          |
| <b>Net operating income before loan<br/>impairment charges and other<br/>credit risk provisions</b> | <b>2,848</b>                               | <b>949</b>                     | <b>462</b>  | <b>29</b>                   | <b>11</b>      | <b>(13)</b>                               | <b>4,286</b>   |
| Loan impairment (charges)/<br>recoveries and other credit risk<br>provisions                        | (701)                                      | (74)                           | 2   |                             | (2)            |   | (775)          |
| <b>Net operating income</b>   | <b>2,147</b>                               | <b>875</b>                     | <b>464</b>  | <b>29</b>                   | <b>9</b>       | <b>(13)</b>                               | <b>3,511</b>   |
| Total operating expenses  | (1,764)                                    | (523)                          | (211)   | (19)                        | (12)           | 13  | (2,516)        |
| <b>Operating profit/(loss)</b>  | <b>383</b>                                 | <b>352</b>                     | <b>253</b>  | <b>10</b>                   | <b>(3)</b>     |   | <b>995</b>     |
| Share of profit in associates and joint<br>ventures   | 5  |                                |   |                             |                |   | 5              |
| <b>Profit/(loss) before tax</b>   | <b>388</b>                                 | <b>352</b>                     | <b>253</b>  | <b>10</b>                   | <b>(3)</b>     |   | <b>1,000</b>   |
|   | %  | %                              | %   | %                           | %              |   | %              |

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|                                   |      |      |      |      |       |      |
|-----------------------------------|------|------|------|------|-------|------|
| Share of HSBC s profit before tax | 2.7  | 2.5  | 1.8  | 0.1  |       | 7.1  |
| Cost efficiency ratio             | 61.9 | 55.1 | 45.7 | 65.5 | 109.1 | 58.7 |

**Balance sheet data<sup>2</sup>**

|  | US\$m  | US\$m  | US\$m  | US\$m | US\$m | US\$m  |
|--|--------|--------|--------|-------|-------|--------|
| Loans and advances to customers (net)  | 19,529 | 12,744 | 8,306  | 27    |       | 40,606 |
| Total assets   | 32,024 | 17,520 | 39,260 | 96    | 25    | 88,925 |
| Customer accounts  | 26,195 | 14,546 | 13,778 | 511   | 219   | 55,249 |
| Loans and advances to banks (net) <sup>3</sup>   |        |        | 10,625 |       |       |        |
| Trading assets, financial instruments designated at fair value, and financial investments <sup>3</sup> |        |        | 17,263 |       |       |        |
| Deposits by banks <sup>3</sup>   |        |        | 2,862  |       |       |        |

For footnotes, see page 72.

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Half-year to 30 June 2006<sup>4</sup>

| <b>Latin America</b>  | Personal<br>Financial<br>Services<br>US\$m | Commercial<br>Banking<br>US\$m | Corporate,<br>Investment<br>Banking &<br>Markets<br>US\$m | Private<br>Banking<br>US\$m | Other<br>US\$m | Inter-<br>segment<br>elimination<br>US\$m | Total<br>US\$m |
|---|--|--------------------------------|---|-----------------------------|----------------|---|----------------|
| Net interest income/ (expense)  | 1,455                                      | 487                            | 185   | 6                           | (2)            | (127)                                     | 2,004          |
| Net fee income  | 496  | 179                            | 88  | 7                           |                |   | 770            |
| Trading income excluding net<br>interest income   | 25   | 12                             | 125   | 1                           |                |   | 163            |
| Net interest income/ (expense) on<br>trading activities   | 2  | 3                              | (37)  |                             |                | 127                                       | 95             |
| Net trading income  | 27   | 15                             | 88  | 1                           |                | 127                                       | 258            |
| Net income from financial<br>instruments designated at fair<br>value                                | 101  |                                | 5   |                             |                |   | 106            |
| Gains less losses from financial<br>investments   | 3  |                                | 35  |                             |                |   | 38             |
| Dividend income   | 3  |                                |   |                             |                |   | 3              |
| Net earned insurance premiums   | 477  | 12                             | 33  |                             |                |   | 522            |
| Other operating income  | 33   | 5                              | 4   | 3                           | 5              | (9)                                       | 41             |
| <b>Total operating income</b>   | <b>2,595</b>                               | <b>698</b>                     | <b>438</b>  | <b>17</b>                   | <b>3</b>       | <b>(9)</b>                                | <b>3,742</b>   |
| Net insurance claims <sup>1</sup>   | (455)                                      | (8)                            | (25)  |                             | (1)            |   | (489)          |
| <b>Net operating income before loan<br/>impairment charges and other<br/>credit risk provisions</b> | <b>2,140</b>                               | <b>690</b>                     | <b>413</b>  | <b>17</b>                   | <b>2</b>       | <b>(9)</b>                                | <b>3,253</b>   |
| Loan impairment (charges)/<br>recoveries and other credit risk<br>provisions                        | (401)                                      | (65)                           | 25  |                             | (1)            |   | (442)          |
| <b>Net operating income</b>   | <b>1,739</b>                               | <b>625</b>                     | <b>438</b>  | <b>17</b>                   | <b>1</b>       | <b>(9)</b>                                | <b>2,811</b>   |
| <b>Total operating expenses</b>   | <b>(1,385)</b>                             | <b>(388)</b>                   | <b>(161)</b>  | <b>(14)</b>                 | <b>(7)</b>     | <b>9</b>                                  | <b>(1,946)</b> |
| <b>Operating profit/(loss)</b>  | <b>354</b>                                 | <b>237</b>                     | <b>277</b>  | <b>3</b>                    | <b>(6)</b>     |   | <b>865</b>     |
| Share of profit in associates and<br>joint ventures   |  |                                |   |                             |                |   |                |
| <b>Profit/(loss) before tax</b>   | <b>354</b>                                 | <b>237</b>                     | <b>277</b>  | <b>3</b>                    | <b>(6)</b>     |   | <b>865</b>     |
|   | %  | %                              | %   | %                           | %              |   | %              |
| Share of HSBC's profit before tax   | 2.8  | 1.9                            | 2.2   |                             |                |   | 6.9            |
| Cost efficiency ratio   | 64.7                                       | 56.2                           | 39.0  | 82.4                        | 350.0          |   | 59.8           |
| <b>Balance sheet data<sup>2</sup></b>   | <b>US\$m</b>                               | <b>US\$m</b>                   | <b>US\$m</b>  | <b>US\$m</b>                | <b>US\$m</b>   |   | <b>US\$m</b>   |
| Loans and advances to customers<br>(net)  | 10,618                                     | 7,403                          | 6,912   | 14                          |                |   | 24,947         |
| Total assets  | 17,812                                     | 9,169                          | 31,923  | 75                          | 18             |   | 58,997         |

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|  |        |        |        |     |        |
|--|--------|--------|--------|-----|--------|
| Customer accounts  | 19,337 | 10,310 | 10,259 | 171 | 40,077 |
| Loans and advances to banks<br>(net) <sup>3</sup>  |        |        | 7,997  |     |        |
| Trading assets, financial<br>instruments designated at fair<br>value, and financial investments <sup>3</sup> |        |        | 14,075 |     |        |
| Deposits by banks <sup>3</sup>   |        |        | 1,652  |     |        |

*For footnotes, see page 72.*

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HSBC HOLDINGS PLC

**Business Review** (continued)

Profit/(loss) before tax and balance sheet data by customer group and global business (continued)

Half-year to 31 December 2006

| <b>Latin America</b>  | Personal<br>Financial<br>Services<br>US\$m | Commercial<br>Banking<br>US\$m | Corporate,<br>Investment<br>Banking &<br>Markets<br>US\$m | Private<br>Banking<br>US\$m | Other<br>US\$m | Inter-<br>segment<br>elimination<br>US\$m | Total<br>US\$m |
|---|--|--------------------------------|---|-----------------------------|----------------|---|----------------|
| Net interest income   | 1,602                                      | 550                            | 140   | 7                           |                | (106)                                     | 2,193          |
| Net fee income  | 557  | 208                            | 79  | 16                          |                |   | 860            |
| Trading income excluding net<br>interest income   | 36   | 9                              | 93  |                             |                |   | 138            |
| Net interest income on trading<br>activities  | 12   | 2                              | 21  |                             |                | 106                                       | 141            |
| Trading income  | 48   | 11                             | 114   |                             |                | 106                                       | 279            |
| Net income/(expense) from<br>financial instruments designated<br>at fair value                      | 126  |                                | 6   |                             | (1)            |   | 131            |
| Gains less losses from financial<br>investments   | 8  | 1                              | 37  |                             |                |   | 46             |
| Dividend income   | 2  | 1                              |   |                             |                |   | 3              |
| Net earned insurance premiums   | 515  | 15                             | 26  |                             | (2)            |   | 554            |
| Other operating income  | 41   | 2                              | 6   | 1                           | 9              | (9)                                       | 50             |
| <b>Total operating income</b>   | <b>2,899</b>                               | <b>788</b>                     | <b>408</b>  | <b>24</b>                   | <b>6</b>       | <b>(9)</b>                                | <b>4,116</b>   |
| Net insurance claims <sup>1</sup>   | (502)                                      | (8)                            | (26)  |                             | 2              |   | (534)          |
| <b>Net operating income<br/>before loan impairment charges<br/>and other credit risk provisions</b> | <b>2,397</b>                               | <b>780</b>                     | <b>382</b>  | <b>24</b>                   | <b>8</b>       | <b>(9)</b>                                | <b>3,582</b>   |
| Loan impairment (charges)/<br>recoveries and other credit risk<br>provisions                        | (363)                                      | (132)                          | 1   |                             | (2)            |   | (496)          |
| <b>Net operating income</b>   | <b>2,034</b>                               | <b>648</b>                     | <b>383</b>  | <b>24</b>                   | <b>6</b>       | <b>(9)</b>                                | <b>3,086</b>   |
| <b>Total operating expenses</b>   | <b>(1,592)</b>                             | <b>(434)</b>                   | <b>(185)</b>  | <b>(13)</b>                 | <b>(5)</b>     | <b>9</b>                                  | <b>(2,220)</b> |
| <b>Operating profit</b>   | <b>442</b>                                 | <b>214</b>                     | <b>198</b>  | <b>11</b>                   | <b>1</b>       |   | <b>866</b>     |
| Share of profit in associates and<br>joint ventures   | 4  |                                |   |                             |                |   | 4              |
| <b>Profit before tax</b>  | <b>446</b>                                 | <b>214</b>                     | <b>198</b>  | <b>11</b>                   | <b>1</b>       |   | <b>870</b>     |

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|                                   | %    | %    | %    | %    | %    | %    |
|-----------------------------------|------|------|------|------|------|------|
| Share of HSBC's profit before tax | 4.7  | 2.2  | 2.1  | 0.1  |      | 9.1  |
| Cost efficiency ratio             | 66.4 | 55.6 | 48.4 | 54.2 | 62.5 | 62.0 |

Balance sheet data<sup>2</sup>

|  | US\$m  | US\$m  | US\$m  | US\$m | US\$m | US\$m  |
|--|--------|--------|--------|-------|-------|--------|
| Loans and advances to customers (net)  | 16,165 | 11,463 | 8,147  | 16    |       | 35,791 |
| Total assets   | 28,053 | 16,244 | 36,333 | 90    | 51    | 80,771 |
| Customer accounts  | 25,200 | 13,754 | 11,685 | 222   |       | 50,861 |
| Loans and advances to banks (net) <sup>3</sup>   |        |        | 9,704  |       |       |        |
| Trading assets, financial instruments designated at fair value, and financial investments <sup>3</sup> |        |        | 15,882 |       |       |        |
| Deposits by banks <sup>3</sup>   |        |        | 3,115  |       |       |        |

1 Net insurance claim incurred and movement in policyholders' liabilities.

2 Third party only.

3 These assets and liabilities were significant to Corporate, Investment Banking and Markets.

4 In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

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HSBC HOLDINGS PLC

**Financial Review**

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| <u>Net income from financial instruments designated at fair value</u>           | <u>80</u>   |
| <u>Gains less losses from financial investments</u>                             | <u>81</u>   |
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HSBC HOLDINGS PLC

**Financial Review** (continued)**Financial summary****Income statement**

|   | Half-year to                      |                          |                                 |
|---|-----------------------------------|--------------------------|---------------------------------|
|   | <b>30 June<br/>2007<br/>US\$m</b> | 30 June<br>2006<br>US\$m | 31<br>December<br>2006<br>US\$m |
| Interest income   | 43,567                            | 35,785                   | 40,094                          |
| Interest expense  | (25,337)                          | (19,054)                 | (22,339)                        |
| Net interest income   | 18,230                            | 16,731                   | 17,755                          |
| Fee income  | 12,488                            | 10,441                   | 10,639                          |
| Fee expense   | (1,993)                           | (2,061)                  | (1,837)                         |
| Net fee income  | 10,495                            | 8,380                    | 8,802                           |
| Trading income excluding net interest income  | 3,351                             | 3,112                    | 2,507                           |
| Net interest income on trading activities   | 2,160                             | 1,149                    | 1,454                           |
| Net trading income  | 5,511                             | 4,261                    | 3,961                           |
| Net income from financial instruments designated at fair value                              | 874                               | 260                      | 397                             |
| Gains less losses from financial investments  | 999                               | 493                      | 476                             |
| Gains arising from dilution of interests in associates                                      | 1,076                             |                          |                                 |
| Dividend income   | 252                               | 222                      | 118                             |
| Net earned insurance premiums   | 3,977                             | 2,834                    | 2,834                           |
| Other operating income  | 678                               | 1,153                    | 1,393                           |
| <b>Total operating income</b>   | <b>42,092</b>                     | <b>34,334</b>            | <b>35,736</b>                   |
| Net insurance claims incurred and movement in policyholders' liabilities                    | (3,599)                           | (2,149)                  | (2,555)                         |
| <b>Net operating income before loan impairment charges and other credit risk provisions</b> | <b>38,493</b>                     | <b>32,185</b>            | <b>33,181</b>                   |
| Loan impairment charges and other credit risk provisions                                    | (6,346)                           | (3,890)                  | (6,683)                         |
| <b>Net operating income</b>   | <b>32,147</b>                     | <b>28,295</b>            | <b>26,498</b>                   |
| Employee compensation and benefits  | (10,430)                          | (8,992)                  | (9,508)                         |
| General and administrative expenses   | (7,022)                           | (6,065)                  | (6,758)                         |
| Depreciation of property, plant and equipment   | (817)                             | (748)                    | (766)                           |
| Amortisation and impairment of intangible assets  | (342)                             | (334)                    | (382)                           |
| <b>Total operating expenses</b>   | <b>(18,611)</b>                   | <b>(16,139)</b>          | <b>(17,414)</b>                 |
| <b>Operating profit</b>   | <b>13,536</b>                     | <b>12,156</b>            | <b>9,084</b>                    |

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|   |                |                |                |
|---|----------------|----------------|----------------|
| Share of profit in associates and joint ventures          | <u>623</u>     | <u>361</u>     | <u>485</u>     |
| <b>Profit before tax</b>                                  | <b>14,159</b>  | 12,517         | 9,569          |
| Tax expense   | <u>(2,645)</u> | <u>(3,272)</u> | <u>(1,943)</u> |
| <b>Profit for the period</b>                              | <b>11,514</b>  | 9,245          | 7,626          |
| Profit attributable to shareholders of the parent company | <b>10,895</b>  | 8,729          | 7,060          |
| Profit attributable to minority interests                 | <b>619</b>     | 516            | 566            |

The economic backdrop to the 2007 interim results was one of solid growth in developed economies and accelerating growth in emerging markets.

Commodity prices and equity markets remained at high levels, and contributed to a continuing high level of financing and merger activity. The number of IPOs remained high, particularly in Asia. The credit environment was benign across the corporate and commercial sectors, while deterioration in retail portfolios was most evident in the US, where the weak housing market remained the major drag on the US economy.

HSBC made a profit before tax of US\$14,159 million, a rise of US\$1,642 million, or 13 per cent, compared with the first half of 2006. Excluding dilution gains arising on the Group's mainland China associates, on an underlying basis profit before tax rose marginally.

Profit growth during the period was overwhelmingly organic and, other than the acquisition of the remaining shares in Erisa in France, there were no significant changes to the constitution of the Group. Integration of previous

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acquisitions progressed satisfactorily in Latin America.

These results were driven by excellent performances across Asia, and in CIBM and Commercial Banking, which offset the effect of higher consumer finance impairment reserves in the US and a challenging environment for the Group's Personal Financial Services business in Europe.

HSBC's results benefited from two specific items. First, a gain of US\$1 billion was recognised in attributable profit as a result of the dilution of the Group's holdings in its mainland China associates. Second, the effective tax rate was unusually low at 18.7 per cent in the period.

The following commentary excludes the effect of the dilution gain.

Revenues grew by US\$5.2 billion, or 16 per cent, compared with cost growth of US\$2.5 billion, or 15 per cent, contributing to an improved cost-efficiency ratio of 49.7 per cent.

Asia drove profit growth, with Hong Kong ahead by 25 per cent and the Rest of Asia-Pacific region by 37 per cent. Latin America and Europe delivered results ahead of the comparable period in 2006 by 16 per cent and 12.5 per cent, respectively. As expected, North America was lower by 35 per cent as a consequence of higher impairment reserves. It is worth noting that HSBC's results for the first half of 2006 benefited from exceptionally low loan impairment charges in the US as a result of changes in local bankruptcy law.

At a customer group and global business level, Commercial Banking delivered pre-tax profits which were 20 per cent ahead of the first half of 2006 and CIBM and Private Banking were 32 per cent and 30 per cent ahead, respectively. HSBC's Personal

Financial Services businesses in Asia also delivered very strong results, with pre-tax profits 38 per cent ahead of the comparable period in 2006. However, overall pre-tax profits within Personal Financial Services declined by 20 per cent compared with the first half of 2006, owing to challenging conditions in the UK and to the weaknesses already highlighted in the Group's US correspondent mortgage business. The actions taken to restructure and reduce exposure in this business are progressing well. The charge for impairments was lower than in the second half of 2006 and, importantly, was in line with management's expectations.

Within these results, the Group's insurance operations made a growing contribution and insurance is seen as a significant growth opportunity for the future.

From a strategic perspective, these results illustrate the value HSBC is creating from its position as the world's largest and most profitable international emerging markets bank, and from its unique global reach, which allows the Group to act as a bridge between developed and developing markets for its customers.

The strong growth HSBC achieved in operating revenues reflects its focus on seeking out growth markets, and has allowed the Group to continue to invest in organic expansion while maintaining a strong capital position and growing dividends to shareholders.

Average invested capital rose by US\$17 billion and the tier one capital ratio remained strong at 9.3 per cent as HSBC pursued expansion around the world. The Group sees this strength as a competitive advantage in light of the current economic environment and the opportunities HSBC sees to deploy capital within its businesses.

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HSBC HOLDINGS PLC

**Financial Review** (continued)**Net interest income**

| By geographical region           | Half-year to |       |              |       |                  |       |
|----------------------------------|--------------|-------|--------------|-------|------------------|-------|
|                                  | 30 June 2007 |       | 30 June 2006 |       | 31 December 2006 |       |
|                                  | US\$m        | %     | US\$m        | %     | US\$m            | %     |
| Europe                           | 3,920        | 21.5  | 4,094        | 24.5  | 4,195            | 23.6  |
| Hong Kong                        | 2,568        | 14.1  | 2,158        | 12.9  | 2,527            | 14.2  |
| Rest of Asia-Pacific             | 1,901        | 10.4  | 1,479        | 8.8   | 1,568            | 8.8   |
| North America <sup>1</sup>       | 7,307        | 40.1  | 6,996        | 41.8  | 7,272            | 41.0  |
| Latin America <sup>1</sup>       | 2,534        | 13.9  | 2,004        | 12.0  | 2,193            | 12.4  |
| Net interest income <sup>2</sup> | 18,230       | 100.0 | 16,731       | 100.0 | 17,755           | 100.0 |

|  | Half-year to |              |                  |
|--|--------------|--------------|------------------|
|  | 30 June 2007 | 30 June 2006 | 31 December 2006 |
|  | US\$m        | US\$m        | US\$m            |
| Net interest income <sup>2</sup>             | 18,230       | 16,731       | 17,755           |
| Average interest-earning assets              | 1,230,903    | 1,081,398    | 1,144,888        |
| Gross interest yield (per cent) <sup>3</sup> | 7.14         | 6.67         | 6.95             |
| Net interest spread (per cent) <sup>4</sup>  | 2.93         | 3.01         | 2.87             |
| Net interest margin (per cent) <sup>5</sup>  | 2.99         | 3.12         | 3.08             |

1 In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

2 Net interest income comprises interest income less interest expense on financial assets and liabilities which is not recognised as part of Net trading income or Net income earned from financial instruments designated at fair value.

3 Gross interest yield is the average annualised interest rate earned on average interest-earning assets (AIEA).

4 Net interest spread is the difference between the average annualised interest rate earned on AIEA and the average annualised interest rate paid on average interest-bearing funds.

5 Net interest margin is net interest income expressed as an annualised percentage of AIEA.

Net interest income of US\$18,230 million was 9 per cent higher than in the first half of 2006, 4 per cent higher on an underlying basis. The commentary below is on an underlying basis.

Movements in net interest income were particularly influenced by the following factors:

- rising short-term interest rates continued to flatten yield curves in most European markets and in the US, restricting opportunities for Global Markets to generate additional income.

This feature was largely mitigated by higher balance sheet management revenues in Hong Kong;

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- interest rate rises in major currencies increased the interest income earned from low-cost deposits and transactional balances, particularly in Personal Financial Services and Commercial Banking. The Group's payments and cash management businesses also benefited from this effect;
- HSBC's reported net interest income includes the funding cost of an increasing proportion of internally funded trading assets, while the related revenue from these is reported in trading income. This is particularly relevant to the UK, France, Hong Kong and the US. The cost of funding net long positions is included within net trading income as an interest expense in HSBC's customer group reporting;
- spreads were squeezed by market conditions in two respects: lending spreads continued to suffer from strong liquidity and benign credit conditions, and liability spreads narrowed from increased competition for core deposits in certain markets; and
- HSBC continued to diversify away from credit-related income streams to more competitive deposit products and, in consequence, customer deposits grew at a rate which exceeded the growth in customer loans.

In Europe, net interest income decreased by 15 per cent. The benefit of balance sheet growth and improved deposit spreads in Personal Financial Services and Commercial Banking was substantially offset by the increased deployment of liabilities to fund trading activity, referred to above; there was a corresponding rise in trading income. This was most pronounced in the UK and France.

In UK Personal Financial Services, balance growth was most significant in savings accounts, owing to a continuing focus on attracting savings balances. Interest income from credit cards decreased, and reduced interest income from unsecured loans reflected HSBC's decision to

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contain growth through stricter underwriting criteria, reflecting its restricted credit appetite. Interest income from mortgages declined as customers sought to fix their monthly payments following the four UK base rate increases between August 2006 and 30 June 2007. In Commercial Banking, strong customer recruitment led to a 9 per cent rise in deposit balances, which helped fund lending growth of 14 per cent. UK balance sheet management revenues declined as the rising trend in short-term interest rates continued to flatten yield curves.

In Hong Kong, net interest income rose by 20 per cent. The benefits from increased lending and deposit balances were augmented by widening deposit spreads as interest rates rose outside Hong Kong, improving income from foreign currency accounts. Growth was strong in Personal Financial Services, with average customer deposits rising by 9 per cent, owing to a competitive pricing strategy and promotional campaigns. Credit card balances increased by 15 per cent, although the associated benefits were partly offset by narrowing mortgage spreads from competitive pressures. Commercial lending and deposit balances grew significantly due to a higher number of customer accounts. Net interest income from CIBM increased significantly as balance sheet management revenues stabilised following a number of periods of decline, and there was strong growth in revenue from deposit products. The increased deployment of these liabilities to fund trading activities, however, reduced reported growth in net interest income, with a corresponding increase in trading income.

In the Rest of Asia-Pacific region, HSBC's ongoing investment in expanding the branch network and its successful marketing campaigns and promotions resulted in growth in customer numbers and so delivered a 24 per cent rise in net interest income. In Personal Financial Services, increased lending balances were funded by strong deposit growth. Strong regional economies, combined with HSBC's continued focus on developing cross-border capabilities, supported growth on both sides of the balance sheet in Commercial Banking. Wider liability spreads from rising interest rates augmented

the income benefits of balance sheet growth. Net interest income was further boosted by notable contributions from the payment and cash management businesses in most countries.

In North America, net interest income increased modestly, benefiting from growth in savings, credit card and personal loan portfolios. Mortgage balances increased slightly, primarily from growth in non-prime balances within the branch-based consumer lending business. The benefits from volume growth were largely offset as asset spreads narrowed due to higher funding costs. Also, deposit spreads suffered from competitive pressures and a change in product mix as customers migrated to higher yielding products. Business expansion and higher volumes from micro, small and mid-market customers resulted in growth in both lending and deposit balances in Commercial Banking. The flat US dollar yield curve resulted in lower balance sheet management revenues, though this was more than offset by increased net interest income from payments and cash management activities due to higher customer balances and lower funding costs on short-term securities. The reduced cost of internal funding, a result of decreased trading activity, further benefited net interest income with a corresponding decrease in trading income.

In Latin America, net interest income rose by 12 per cent. A continuing favourable economic climate, combined with increased sales and marketing activity, led to robust growth in lending and deposit balances. In Mexico, average credit card balances rose by 124 per cent due to strong customer acquisition supported by promotional campaigns. The benefits from balance sheet growth and improved asset spreads were partly offset by the adverse effect of a flat yield curve on balance sheet management activity in Mexico. Net interest income in Brazil increased as a positive economic outlook and falling interest rates led to strong demand for credit.

Average interest earning assets of US\$1,231 billion were US\$150 billion, or 14 per cent, higher than in the first half of 2006 on an underlying basis.

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HSBC HOLDINGS PLC

**Financial Review** (continued)**Net fee income**

| By geographical region     | Half-year to |       |              |       |                  |       |
|----------------------------|--------------|-------|--------------|-------|------------------|-------|
|                            | 30 June 2007 |       | 30 June 2006 |       | 31 December 2006 |       |
|                            | US\$m        | %     | US\$m        | %     | US\$m            | %     |
| Europe                     | 4,144        | 39.5  | 3,513        | 41.9  | 3,595            | 40.8  |
| Hong Kong                  | 1,439        | 13.7  | 1,000        | 11.9  | 1,056            | 12.0  |
| Rest of Asia-Pacific       | 1,010        | 9.6   | 785          | 9.4   | 837              | 9.5   |
| North America <sup>1</sup> | 2,904        | 27.7  | 2,312        | 27.6  | 2,454            | 27.9  |
| Latin America <sup>1</sup> | 998          | 9.5   | 770          | 9.2   | 860              | 9.8   |
| Net fee income             | 10,495       | 100.0 | 8,380        | 100.0 | 8,802            | 100.0 |

|  | Half-year to |              |                  |
|--|--------------|--------------|------------------|
|  | 30 June 2007 | 30 June 2006 | 31 December 2006 |
|  | US\$m        | US\$m        | US\$m            |
| Cards                                  | 3,092        | 2,482        | 2,885            |
| Account services                       | 1,961        | 1,688        | 1,945            |
| Funds under management                 | 1,390        | 1,571        | 1,147            |
| Broking income                         | 928          | 728          | 626              |
| Insurance                              | 804          | 693          | 665              |
| Credit facilities                      | 672          | 462          | 460              |
| Global custody                         | 557          | 423          | 374              |
| Unit trusts                            | 420          | 265          | 255              |
| Imports/exports                        | 407          | 383          | 397              |
| Remittances                            | 273          | 223          | 249              |
| Corporate finance                      | 220          | 95           | 160              |
| Underwriting                           | 196          | 150          | 136              |
| Trust income                           | 146          | 113          | 135              |
| Maintenance income on operating leases | 69           | 59           | 63               |
| Mortgage servicing                     | 53           | 47           | 50               |
| Other                                  | 1,300        | 1,059        | 1,092            |
| Total fee income                       | 12,488       | 10,441       | 10,639           |
| Less: fee expense                      | (1,993)      | (2,061)      | (1,837)          |

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|                |                            |                            |                            |
|----------------|----------------------------|----------------------------|----------------------------|
| Net fee income | <b>10,495</b>              | 8,380                      | 8,802                      |
|                | <hr style="width: 100%;"/> | <hr style="width: 100%;"/> | <hr style="width: 100%;"/> |

1 *In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.*

Net fee income rose by 25 per cent to US\$10,495 million, compared with US\$8,380 million in the first half of 2006. On an underlying basis, net fee income rose by 21 per cent. The principal drivers of this growth were as follows:

- broking income, global custody fees and unit trust fees rose as a result of strong equity markets, particularly in Hong Kong, the UK, Germany, South Korea and India. Additional performance fees were earned on emerging markets funds. In Hong Kong, an emphasis on wealth management products and fees from cash management and remittances coincided with increased activity in both equity and currency markets and a rise in trade flows. Investment banking opportunities arose in Asia from the large number of IPOs, and in Europe from increased market activity, particularly in the UK and France;
- increased personal credit card transaction volumes and balances led to a 14 per cent increase in card fee income, predominantly in the US, but also in Mexico, Turkey and the Middle East. In the US retail services business, customer account balances were maintained at high levels, which generated additional fee income from payments. The bundling of cards with other products, such as Tu Cuenta Mexico, and acquisition campaigns contributed to the increased number of cards issued and resulted in higher balances;
- insurance sales improved on the back of strong demand in the US and improved distribution capabilities in Asia and Latin America;
- account service fees and credit services fees grew by 44 per cent in the US and by 21 per cent in Latin America. Transaction volumes and customer numbers increased, while revised pricing structures proved beneficial to growth in



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net fee income. In the UK, fees related to credit facilities increased; and

- credit-related fees grew strongly in CIBM from successful implementation of its emerging markets-led, financing-focused strategy.

**Net trading income**

| By geographical region     | Half-year to |              |              |              |                  |              |
|----------------------------|--------------|--------------|--------------|--------------|------------------|--------------|
|                            | 30 June 2007 |              | 30 June 2006 |              | 31 December 2006 |              |
|                            | US\$m        | %            | US\$m        | %            | US\$m            | %            |
| Europe                     | 3,338        | 60.5         | 2,187        | 51.4         | 2,342            | 59.1         |
| Hong Kong                  | 469          | 8.5          | 306          | 7.2          | 311              | 7.9          |
| Rest of Asia-Pacific       | 797          | 14.5         | 551          | 12.9         | 630              | 15.9         |
| North America <sup>1</sup> | 622          | 11.3         | 959          | 22.5         | 399              | 10.1         |
| Latin America <sup>1</sup> | 285          | 5.2          | 258          | 6.0          | 279              | 7.0          |
| <b>Net trading income</b>  | <b>5,511</b> | <b>100.0</b> | <b>4,261</b> | <b>100.0</b> | <b>3,961</b>     | <b>100.0</b> |

|   | Half-year to |              |                  |
|---|--------------|--------------|------------------|
|   | 30 June 2007 | 30 June 2006 | 31 December 2006 |
|   | US\$m        | US\$m        | US\$m            |
| Trading activities                          | 3,266        | 3,055        | 2,410            |
| Net interest income on trading activities   | 2,160        | 1,149        | 1,454            |
| Other trading income Hedge ineffectiveness: |              |              |                  |
| on cash flow hedges                         | (49)         | (46)         | (76)             |
| on fair value hedges                        | 21           | (11)         | 27               |
| Non-qualifying hedges                       | 113          | 114          | 146              |
| <b>Net trading income</b>                   | <b>5,511</b> | <b>4,261</b> | <b>3,961</b>     |

<sup>1</sup> In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

Net trading income increased by 29 per cent, reflecting continued business growth, favourable market conditions, and the investments made in extending Global Markets product range and enhancing its sales and execution capabilities. The cost of internal funding on long positions is excluded from the reported Net trading income line and included in Net interest income. However, this cost is reinstated in Net trading income in HSBC's customer group and global business reporting.

Income from structured derivatives grew by 53 per cent, as recent investments in technical expertise and systems enabled HSBC to address a broader spectrum of client needs. Advantage was taken of volatile market conditions to grow net trading income and structured equity and structured credit derivatives volumes grew as a result of increased transactions with clients.

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Record foreign exchange income was reported in the first half of 2007, with strong results in Hong

Kong, Rest of Asia-Pacific and Latin America. In aggregate, foreign exchange income in Asia and Latin America increased by 25 per cent, reflecting the benefits of CIBM's focus on emerging markets and improved leverage from HSBC's strong and diversified distribution network.

Within the credit and rates business, trading income declined as performance was negatively affected by conditions in the sub-prime mortgage market, which resulted in the widening of credit spreads.

Equities income grew by 52 per cent, with record results achieved in the period. Trading income growth was underpinned by the strength of major stock indices, with further growth driven by equity financing and equity derivatives. In France, the business benefited from a gain of US\$93 million from the sale of an investment in Euronext N.V. shares.

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HSBC HOLDINGS PLC

**Financial Review** (continued)**Net income from financial instruments designated at fair value**

|                               | Half-year to<br>30 June 2007 |              | At<br>30 June 2007 |                      |
|-------------------------------|------------------------------|--------------|--------------------|----------------------|
|                               | Net income<br>US\$m          | %            | Assets<br>US\$m    | Liabilities<br>US\$m |
| <b>By geographical region</b> |                              |              |                    |                      |
| Europe                        | 348                          | 39.8         | 24,936             | 36,749               |
| Hong Kong                     | 210                          | 24.0         | 5,507              | 4,393                |
| Rest of Asia-Pacific          | 78                           | 8.9          | 1,836              | 480                  |
| North America <sup>1</sup>    | 81                           | 9.3          |                    | 34,344               |
| Latin America <sup>1</sup>    | 157                          | 18.0         | 2,570              |                      |
|                               | <b>874</b>                   | <b>100.0</b> | <b>34,849</b>      | <b>75,966</b>        |

|                               | Half-year to<br>30 June 2006  |              | At<br>30 June 2006 |                      |
|-------------------------------|-------------------------------|--------------|--------------------|----------------------|
|                               | Net income/(expense)<br>US\$m | %            | Assets<br>US\$m    | Liabilities<br>US\$m |
| <b>By geographical region</b> |                               |              |                    |                      |
| Europe                        | 129                           | 49.6         | 10,561             | 28,649               |
| Hong Kong                     | 6                             | 2.3          | 4,000              | 4,067                |
| Rest of Asia-Pacific          | (5)                           | (1.9)        | 854                | 307                  |
| North America <sup>1</sup>    | 24                            | 9.2          |                    | 31,143               |
| Latin America <sup>1</sup>    | 106                           | 40.8         | 1,440              | 188                  |
|                               | <b>260</b>                    | <b>100.0</b> | <b>16,855</b>      | <b>64,354</b>        |

|                               | Half-year to<br>31 December 2006 |        | At<br>31 December 2006 |                      |
|-------------------------------|----------------------------------|--------|------------------------|----------------------|
|                               | Net income/(expense)<br>US\$m    | %      | Assets<br>US\$m        | Liabilities<br>US\$m |
| <b>By geographical region</b> |                                  |        |                        |                      |
| Europe                        | 15                               | 3.8    | 12,164                 | 32,630               |
| Hong Kong                     | 254                              | 64.0   | 4,745                  | 4,291                |
| Rest of Asia-Pacific          | 84                               | 21.2   | 1,729                  | 410                  |
| North America                 | (87)                             | (22.0) |                        | 32,880               |

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|               |            |              |               |               |
|---------------|------------|--------------|---------------|---------------|
| Latin America | 131        | 33.0         | 1,935         |               |
|               | <u>397</u> | <u>100.0</u> | <u>20,573</u> | <u>70,211</u> |

Half-year to

|  | <b>30 June<br/>2007<br/>US\$m</b> | 30 June<br>2006<br>US\$m | 31 December<br>2006<br>US\$m |
|--|-----------------------------------|--------------------------|------------------------------|
| Income from assets held to meet liabilities under insurance and investment contracts | <b>1,348</b>                      | 318                      | 1,234                        |
| Change in fair value of liabilities to customers under investment contracts          | <b>(620)</b>                      | (226)                    | (782)                        |
| Movement in fair value of HSBC's long-term debt issued and related derivatives       | <b>284</b>                        | 135                      | (170)                        |
| change in own credit spread on long-term debt  | <b>172</b>                        | (172)                    | (216)                        |
| other changes in fair value  | <b>112</b>                        | 307                      | 46                           |
| Income/(expense) from other instruments designated at fair value                     | <b>(138)</b>                      | 33                       | 115                          |
| Net income from financial instruments designated at fair value                       | <b>874</b>                        | 260                      | 397                          |

1 In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

HSBC has principally used the fair value designation in the following instances:

- for certain fixed-rate long-term debt issues whose interest rate characteristic has been changed to floating through interest rate swaps as part of a documented interest rate management strategy. Approximately US\$61 billion of the Group's debt issues have been accounted for using the fair value option. The movement in fair value of these debt issues includes the effect of own credit spread changes and any ineffectiveness in the economic relationship between the related swaps and own

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debt. As credit spreads narrow, accounting losses are booked, and the reverse is true in the event of spreads widening. Ineffectiveness arises from the different credit characteristics of the swap and own debt coupled with the sensitivity of the floating leg of the swap to changes in short-term interest rates. The size and direction of the accounting consequences of changes in own credit spread and ineffectiveness can be volatile from period to period, but do not alter the cash flows envisaged as part of the documented interest rate management strategy;

- for certain financial assets held by insurance operations and managed at fair value to meet liabilities under insurance contracts (approximately US\$7 billion of assets); and
- for financial liabilities under investment contracts and the related financial assets, when the change in value of the assets is correlated with the change in value of the liabilities to policyholders (approximately US\$18 billion of assets and related liabilities).

Net income from assets designated at fair value and held to meet liabilities under insurance and investment contracts is correlated with changes in liabilities under the related investment and insurance contracts. Liabilities under investment contracts are generally measured at fair value and changes are taken to Net income from financial instruments designated at fair value to match the net income on

the related assets. There is, however, a mismatch in presentation for insurance contracts where the change in the value of the insurance contract liabilities is included within Net insurance claims incurred and movement in policyholders' liabilities, whereas any related asset returns are included within Net income from financial instruments designated at fair value.

The commentary that follows is on an underlying basis.

Net income from financial instruments designated at fair value increased by 112 per cent compared with the first half of 2006. Income from assets held to meet liabilities under insurance and investment contracts rose by 201 per cent, mostly from higher investment returns in equity portfolios held by insurance companies in the UK and Hong Kong. The change in fair value of liabilities under investment contracts increased by 159 per cent compared with the first half of 2006, reflecting the attribution to customers of the majority of the gain on investment contract assets.

The remainder of the increase reflected a widening of credit spreads on certain fixed-rate long-term debt issued by HSBC Finance and higher net mark-to-market movements on this debt, partly offset by mark-to-market losses on the related interest rate swaps. This gain reversed losses taken in prior periods and, over the life of this debt, these fair value adjustments will fully reverse.

### Gains less losses from financial investments

|  | Half-year to |       |              |       |                  |       |
|--|--------------|-------|--------------|-------|------------------|-------|
|  | 30 June 2007 |       | 30 June 2006 |       | 31 December 2006 |       |
|  | US\$m        | %     | US\$m        | %     | US\$m            | %     |
| <b>By geographical region</b>                |              |       |              |       |                  |       |
| Europe                                       | 790          | 79.1  | 266          | 54.0  | 358              | 75.2  |
| Hong Kong                                    | 32           | 3.2   | 122          | 24.7  | 40               | 8.4   |
| Rest of Asia-Pacific                         | 26           | 2.6   | 27           | 5.5   | 14               | 2.9   |
| North America <sup>1</sup>                   | 53           | 5.3   | 40           | 8.1   | 18               | 3.8   |
| Latin America <sup>1</sup>                   | 98           | 9.8   | 38           | 7.7   | 46               | 9.7   |
| Gains less losses from financial investments | 999          | 100.0 | 493          | 100.0 | 476              | 100.0 |

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Half-year to

|  | <b>30 June</b> | 30 June | 31 December |
|--|----------------|---------|-------------|
|  | <b>2007</b>    | 2006    | 2006        |
|  | <b>US\$m</b>   | US\$m   | US\$m       |
| Net gains from disposal of:                  |                |         |             |
| debt securities                              | <b>133</b>     | 154     | 98          |
| equity securities                            | <b>852</b>     | 338     | 364         |
| other financial investments                  | <b>14</b>      | 1       | 14          |
|  | <b>999</b>     | 493     | 476         |
| Gains less losses from financial investments | <b>999</b>     | 493     | 476         |

1 *In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.*

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HSBC HOLDINGS PLC

**Financial Review** (continued)

HSBC reported net gains of US\$999 million from the disposal of available-for-sale financial investments during the first half of 2007, 103 per cent higher than in the first half of 2006. Gains from financial instruments were primarily attributable to the gain on the sale of shareholdings and the successful realisation of a number of private equity investments in both the UK and France. In Latin America, a gain arose from the sale of Serasa, a credit bureau.

In the first half of 2006, HSBC benefited from a US\$93 million gain arising from the partial redemption of HSBC's investment in MasterCard Incorporated following its IPO and a gain of US\$101 million on the sale of part of HSBC's stake in UTI Bank Limited, which did not recur in 2007.

**Gains arising from dilution of interests in associates**

Three of HSBC's associates, Industrial Bank, Ping An Insurance and Bank of Communications, issued new shares for which HSBC did not subscribe. As a consequence of the new monies raised by the associates, HSBC's share of their underlying assets increased by US\$1,076 million, notwithstanding the reduction in the Group's interests. These gains are presented in the income statement as Gains from dilution of the Group's interests in associates, and should be regarded as exceptional. For further details see Note 19 on the Financial Statements.

**Net earned insurance premiums**

|                               | Half-year to |       |              |       |                  |       |
|-------------------------------|--------------|-------|--------------|-------|------------------|-------|
|                               | 30 June 2007 |       | 30 June 2006 |       | 31 December 2006 |       |
|                               | US\$m        | %     | US\$m        | %     | US\$m            | %     |
| <b>By geographical region</b> |              |       |              |       |                  |       |
| Europe                        | 1,480        | 37.2  | 668          | 23.6  | 630              | 22.2  |
| Hong Kong                     | 1,426        | 35.9  | 1,317        | 46.5  | 1,311            | 46.3  |
| Rest of Asia-Pacific          | 109          | 2.7   | 89           | 3.1   | 85               | 3.0   |
| North America <sup>1</sup>    | 231          | 5.8   | 238          | 8.4   | 254              | 9.0   |
| Latin America <sup>1</sup>    | 731          | 18.4  | 522          | 18.4  | 554              | 19.5  |
| Net earned insurance premiums | 3,977        | 100.0 | 2,834        | 100.0 | 2,834            | 100.0 |

|                                | Half-year to |              |                  |
|--------------------------------|--------------|--------------|------------------|
|                                | 30 June 2007 | 30 June 2006 | 31 December 2006 |
|                                | US\$m        | US\$m        | US\$m            |
| Gross insurance premium income | 4,532        | 3,262        | 3,193            |

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|                               |       |       |       |
|-------------------------------|-------|-------|-------|
| Reinsurance premiums          | (555) | (428) | (359) |
| Net earned insurance premiums | 3,977 | 2,834 | 2,834 |

1 *In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.*

Net earned insurance premiums of US\$3,977 million were US\$1,143 million, or 40 per cent, higher than in the first half of 2006. During the year, HSBC acquired the remaining shares in Erisa in France. Net earned insurance premiums increased by 10 per cent on an underlying basis.

The commentary that follows is on an underlying basis.

In Europe, net earned insurance premiums increased by 1 per cent to US\$1,480 million. Increased premium income from pension fund products in the UK was largely offset by the adverse effect on premiums of HSBC having ceased underwriting certain life insurance products.

In Hong Kong, net earned insurance premiums of US\$1,426 million were 9 per cent higher than in the first half of 2006. Improved premium income from the life business was primarily attributable to an increase in new business, driven by the launch of investment linked insurance products for personal and commercial clients and new propositions designed to meet customers' financial retirement needs.

In the Rest of Asia-Pacific region, net earned insurance premiums were 16 per cent higher than in the first half of 2006. The development of new insurance product initiatives, including a recently launched medical insurance product in Singapore, *shariah*-compliant insurance propositions in the Middle East and the establishment of a *Takaful* joint



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venture in Malaysia, underlined HSBC's continued emphasis on expanding insurance business across the region.

In North America, premium income stayed broadly in line with the first half of 2006.

In Latin America, net earned insurance premiums increased by 28 per cent. In Brazil, pension sales increased and higher personal loan sales resulted in a significant rise in new life business volumes due to life contracts being offered to customers as a complementary product.

**Other operating income**

|                               | Half-year to |              |              |              |                  |              |
|-------------------------------|--------------|--------------|--------------|--------------|------------------|--------------|
|                               | 30 June 2007 |              | 30 June 2006 |              | 31 December 2006 |              |
|                               | US\$m        | %            | US\$m        | %            | US\$m            | %            |
| <b>By geographical region</b> |              |              |              |              |                  |              |
| Europe                        | 262          | 17.1         | 633          | 35.8         | 795              | 35.0         |
| Hong Kong                     | 413          | 27.0         | 443          | 25.0         | 391              | 17.2         |
| Rest of Asia-Pacific          | 360          | 23.5         | 288          | 16.3         | 477              | 21.0         |
| North America <sup>1</sup>    | 342          | 22.4         | 365          | 20.6         | 557              | 24.6         |
| Latin America <sup>1</sup>    | 153          | 10.0         | 41           | 2.3          | 50               | 2.2          |
|                               | <b>1,530</b> | <b>100.0</b> | <b>1,770</b> | <b>100.0</b> | <b>2,270</b>     | <b>100.0</b> |
| Intra-HSBC elimination        | (852)        |              | (617)        |              | (877)            |              |
| Other operating income        | <b>678</b>   |              | <b>1,153</b> |              | <b>1,393</b>     |              |

|  | Half-year to |              |                  |
|--|--------------|--------------|------------------|
|  | 30 June 2007 | 30 June 2006 | 31 December 2006 |
|  | US\$m        | US\$m        | US\$m            |
| Rent received  | 315          | 340          | 347              |
| Gain/(loss) on disposal of assets held for resale                                | (37)         | 79           | (51)             |
| Valuation gains on investment properties   | 48           | 80           | 84               |
| Gain on disposal of property, plant and equipment, and non-financial investments | 152          | 180          | 601              |
| Change in present value of in-force long-term insurance business                 | (155)        | 57           | (17)             |
| Other  | 355          | 417          | 429              |
| Other operating income   | <b>678</b>   | <b>1,153</b> | <b>1,393</b>     |

<sup>1</sup> In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

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Other operating income of US\$678 million was US\$475 million, or 41 per cent, lower than in the first half of 2006, a 49 per cent decline on an underlying basis.

The commentary that follows is on an underlying basis.

In Europe, a 68 per cent decline in other operating income arose due to a fall in the present value of in-force long-term business in the UK which followed a change in FSA regulations. This was more than offset by a reduction in provisions reported in Net insurance claims incurred and movements in policyholders' liabilities. The non-recurrence of the profit realised on the sale of HSBC's stake in The Cyprus Popular Bank contributed further to the decrease.

In Hong Kong, the reduction in other operating income was partly due to the disposal of Hang Seng Bank Limited's former head office building in 2006.

Other operating income in Rest of Asia-Pacific rose by 20 per cent, mostly due to increased levels of activity at the Group Service Centres in India.

In North America, the reduction reflected losses on asset sales following branch closures in the mortgage services business. Income in the retail services business also declined, but these effects were partly mitigated by lower losses on the sale of foreclosed assets, and a gain following a sale and leaseback transaction of a building formerly owned by HSBC's US bank.

In Latin America, the rise in other operating income was mostly driven by a refinement of the income recognition methodology in respect of long-term insurance contracts in Mexico. A gain on a credit card portfolio sale in Brazil contributed further to the increase.

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**Financial Review** (continued)**Net insurance claims incurred and movement in policyholders liabilities**

|   | Half-year to |       |              |       |                  |       |
|---|--------------|-------|--------------|-------|------------------|-------|
|   | 30 June 2007 |       | 30 June 2006 |       | 31 December 2006 |       |
|   | US\$m        | %     | US\$m        | %     | US\$m            | %     |
| <b>By geographical region</b>   |              |       |              |       |                  |       |
| Europe  | 1,146        | 31.8  | 287          | 13.4  | 244              | 9.5   |
| Hong Kong   | 1,512        | 42.1  | 1,193        | 55.5  | 1,506            | 58.9  |
| Rest of Asia-Pacific  | 141          | 3.9   | 63           | 2.9   | 129              | 5.0   |
| North America <sup>1</sup>  | 124          | 3.4   | 117          | 5.4   | 142              | 5.6   |
| Latin America <sup>1</sup>  | 676          | 18.8  | 489          | 22.8  | 534              | 21.0  |
| Net insurance claims incurred and movement in policyholders liabilities | 3,599        | 100.0 | 2,149        | 100.0 | 2,555            | 100.0 |

|   | Half-year to |              |                  |
|---|--------------|--------------|------------------|
|   | 30 June 2007 | 30 June 2006 | 31 December 2006 |
|   | US\$m        | US\$m        | US\$m            |
| Gross insurance claims and movement in policyholders liabilities              | 3,428        | 2,270        | 2,802            |
| Reinsurers share of claims incurred and movement in policyholders liabilities | 171          | (121)        | (247)            |
| Net insurance claims incurred and movement in policyholders liabilities       | 3,599        | 2,149        | 2,555            |

<sup>1</sup> In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

Net insurance claims incurred and movement in policyholders liabilities of US\$3,599 million were 67 per cent higher than in the first half of 2006. During the year, HSBC acquired the remaining shares in Erisa in France. Net insurance claims incurred and movement in policyholders liabilities increased by 13 per cent on an underlying basis.

Net insurance claims incurred and movement in policyholders liabilities arise from both life and non-life insurance business. For non-life business, amounts reported represent the cost of claims paid during the year and the estimated cost of notified claims. For life business, the main element of claims is the liability to policyholders created on the initial underwriting of the policy and any subsequent movement in the liability that arises, primarily from the attribution of investment performance to savings-related policies. Consequently, claims rise in line with increases in sales of savings-related business and with investment market growth.

The commentary that follows is on an underlying basis.

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In Europe, net insurance claims incurred and movement in policyholders' liabilities decreased by 91 per cent, primarily driven by a reduction in the present value of the in-force insurance business, reflecting a change in FSA rules. This was partly offset by a decrease in other operating income.

In Hong Kong, the 28 per cent increase largely reflected higher life insurance premiums in line with business growth.

In Rest of Asia-Pacific, a 110 per cent increase was mainly the result of strong demand for insurance products in Singapore and the launch of HSBC Amanah Takaful in 2006.

In North America, net insurance claims incurred and movement in policyholders' liabilities were broadly in line with the first half of 2006.

In Latin America, higher sales of life and pension fund products, primarily driven by the success of a sales campaign during the first quarter of 2007, led to an increase in net insurance claims.

&lt;

[Back to Contents](#)**Loan impairment charges and other credit risk provisions**

|   | Half-year to |              |              |              |                  |              |
|---|--------------|--------------|--------------|--------------|------------------|--------------|
|   | 30 June 2007 |              | 30 June 2006 |              | 31 December 2006 |              |
|   | US\$m        | %            | US\$m        | %            | US\$m            | %            |
| <b>By geographical region</b>                                   |              |              |              |              |                  |              |
| Europe  | 1,363        | 21.5         | 935          | 24.0         | 1,220            | 18.3         |
| Hong Kong   | 80           | 1.3          | 70           | 1.8          | 102              | 1.5          |
| Rest of Asia-Pacific  | 308          | 4.8          | 271          | 7.0          | 241              | 3.6          |
| North America <sup>1</sup>                                      | 3,820        | 60.2         | 2,172        | 55.8         | 4,624            | 69.2         |
| Latin America <sup>1</sup>                                      | 775          | 12.2         | 442          | 11.4         | 496              | 7.4          |
| <b>Loan impairment charges and other credit risk provisions</b> | <b>6,346</b> | <b>100.0</b> | <b>3,890</b> | <b>100.0</b> | <b>6,683</b>     | <b>100.0</b> |

|   | Half-year to |              |                  |
|---|--------------|--------------|------------------|
|   | 30 June 2007 | 30 June 2006 | 31 December 2006 |
|   | US\$m        | US\$m        | US\$m            |
| <b>Loan impairment charges</b>                                  |              |              |                  |
| New allowances net of allowance releases                        | 6,635        | 4,239        | 7,087            |
| Recoveries of amounts previously written off                    | (307)        | (343)        | (436)            |
|   | <b>6,328</b> | <b>3,896</b> | <b>6,651</b>     |
| Individually assessed allowances                                | 385          | 178          | 280              |
| Collectively assessed allowances                                | 5,943        | 3,718        | 6,371            |
| Other credit risk provisions                                    | 18           | (6)          | 32               |
| <b>Loan impairment charges and other credit risk provisions</b> | <b>6,346</b> | <b>3,890</b> | <b>6,683</b>     |

**At end of period**

|                                     |        |        |        |
|-------------------------------------|--------|--------|--------|
| Customer impaired loans             | 14,555 | 12,296 | 13,785 |
| Customer loan impairment allowances | 14,323 | 11,381 | 13,578 |

<sup>1</sup> In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

Loan impairment charges and other credit risk provisions rose by 63 per cent compared with the first half of 2006, to US\$6,346 million. On an underlying basis, charges increased by 57 per cent. The following factors drove the underlying increase:

- Personal Financial Services, which accounted for the majority of the customer loan portfolio, contributed 91 per cent of the increase. The vast majority of this increase was in North America. Outside North America, the rise in impairment charges reflected portfolio growth and seasoning;
- in assessing the period-on-period increase in loan impairment charges in North America, the following background perspective is important.

The loan impairment charge in the first half of 2006 benefited from:

exceptionally low levels of personal bankruptcy filings in the US, as a result of a new bankruptcy law which took effect in October 2005;

the effect of significant loan growth in 2004 and 2005, which had not yet fully seasoned; and

a generally favourable credit environment in the US which affected the comparability of loan impairment charges between periods.

The increased loan impairment charge in the first half of 2007 reflected higher levels of receivables, higher levels of delinquency driven by normal portfolio seasoning, increased levels of personal bankruptcy filings and the progression of portions of HSBC Finance's mortgage services portfolio purchased in 2005 and 2006 into various stages of delinquency and charge-off;

- in Latin America, a 52 per cent increase in loan impairment charges reflected the rate of underlying growth in lending across the region;
- increased loan impairment charges in the UK arose from a refinement of the roll rate methodology in the consumer finance business and upward market trends in personal bankruptcies and IVAs; and
- the commercial and corporate credit environment in all regions remained largely benign.

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HSBC HOLDINGS PLC

## Financial Review (continued)

The commentary that follows is on an underlying basis.

In Europe, net loan impairment charges increased by 35 per cent, primarily in the UK. In addition to the factors noted above, UK retail impairment charges reflected growth in credit card lending. As a result of the rising market trends in personal bankruptcies and IVAs, HSBC curtailed lending to some higher-risk borrower segments. Corporate credit quality in the UK was broadly stable, with net recoveries in CIBM.

Credit quality in France and Turkey was largely stable. In France, CIBM returned to a small net charge position, compared with net recoveries in the first half of 2006. In Turkey, rising loan impairment charges in Commercial Banking were partly offset by a lower charge in Personal Financial Services.

In Hong Kong, net loan impairment charges were low but rose moderately following lower releases and recoveries compared with the first half of 2006. Generally, credit quality remained sound.

In Rest of Asia-Pacific, net loan impairment charges increased, primarily as a result of increased lending volumes but, in aggregate, remained at low levels. Charges in Thailand rose, due to a single corporate customer, but these were partly offset by releases of previously established impairment allowances against credit card lending in Taiwan and reduced loan impairment charges due to improved delinquency rates on credit cards in Indonesia. In Malaysia, HSBC experienced increased loan impairment charges on mortgage balances in Personal Financial Services due to rising interest rates, and on a single corporate account. Commercial recoveries in the United Arab Emirates were indicative of the generally favourable credit environment in the Middle East. Loan impairment charges in India rose due mainly to increased personal lending, while in mainland China charges were low as a result of improved credit performance in commercial lending.

In North America, net loan impairment charges were significantly higher than in the first half of

2006. The increase predominantly related to the US, but Canada and Bermuda also reported higher loan impairment charges. In the US, the rise reflected recent asset growth, increased delinquency rates as a result of normal portfolio seasoning and the progression of mortgage services portfolios purchased in 2005 and 2006 into various stages of delinquency and write-off. The increase was also attributable to a higher proportion of unsecured loans such as credit cards and personal lending and a return to higher levels of personal insolvency following the lower rates experienced in 2006. The rise in delinquency rates within the mortgage services business, following deterioration in second lien and some first lien mortgages acquired from correspondents, slowed during 2007 compared with the rate of increase during the full year of 2006. Impairment charges in Canada reflected strong asset growth and higher delinquency rates in the motor vehicle finance business. In Bermuda, the movement between reporting periods reflected the non-recurrence of a recovery related to a single corporate client.

In Latin America, recent growth in unsecured lending led to a 52 per cent increase in net loan impairment charges. This rise was primarily concentrated in Mexico, where significant growth in credit card and self-employed lending balances, areas in which HSBC traditionally had a low market presence, led to the rise in loan impairment charges. Loan underwriting criteria and collections strategies are regularly reviewed to maintain the quality of the portfolio.

The aggregate customer loan impairment allowances at 30 June 2007 of US\$14,323 million represented 1.6 per cent of gross customer advances (net of reverse repos, settlement accounts and netting) compared with 1.4 per cent at 30 June 2006.

Impaired loans to customers were US\$14,555 million at 30 June 2007, compared with US\$13,785 million at 31 December 2006. At constant exchange rates, impaired loans increased by 4 per cent compared with 30 June 2006, while underlying lending growth (excluding lending to the financial sector and settlement accounts) was 5 per cent.





[Back to Contents](#)**Operating expenses**

|                               | Half-year to  |              |               |              |                  |              |
|-------------------------------|---------------|--------------|---------------|--------------|------------------|--------------|
|                               | 30 June 2007  |              | 30 June 2006  |              | 31 December 2006 |              |
|                               | US\$m         | %            | US\$m         | %            | US\$m            | %            |
| <b>By geographical region</b> |               |              |               |              |                  |              |
| Europe                        | 7,972         | 40.9         | 6,723         | 40.1         | 7,148            | 39.1         |
| Hong Kong                     | 1,665         | 8.6          | 1,504         | 9.0          | 1,765            | 9.7          |
| Rest of Asia-Pacific          | 2,075         | 10.7         | 1,609         | 9.6          | 1,939            | 10.6         |
| North America1                | 5,235         | 26.9         | 4,974         | 29.7         | 5,219            | 28.5         |
| Latin America1                | 2,516         | 12.9         | 1,946         | 11.6         | 2,220            | 12.1         |
|                               | <b>19,463</b> | <b>100.0</b> | <b>16,756</b> | <b>100.0</b> | <b>18,291</b>    | <b>100.0</b> |
| Intra-HSBC elimination        | (852)         |              | (617)         |              | (877)            |              |
| Operating expenses            | <b>18,611</b> |              | <b>16,139</b> |              | <b>17,414</b>    |              |

|  | Half-year to  |               |                  |
|--|---------------|---------------|------------------|
|  | 30 June 2007  | 30 June 2006  | 31 December 2006 |
|  | US\$m         | US\$m         | US\$m            |
| <b>By expense category</b>                       |               |               |                  |
| Employee compensation and benefits2              | 10,430        | 8,992         | 9,508            |
| Premises and equipment (excluding depreciation)  | 1,848         | 1,640         | 1,749            |
| General and administrative expenses              | 5,174         | 4,425         | 5,009            |
| Administrative expenses                          | 17,452        | 15,057        | 16,266           |
| Depreciation of property, plant and equipment    | 817           | 748           | 766              |
| Amortisation and impairment of intangible assets | 342           | 334           | 382              |
| Operating expenses                               | <b>18,611</b> | <b>16,139</b> | <b>17,414</b>    |

|   | At           | At           | At               |
|---|--------------|--------------|------------------|
|   | 30 June 2007 | 30 June 2006 | 31 December 2006 |
|   |              |              |                  |
| <b>Staff numbers (full-time equivalent)</b> |              |              |                  |
| Europe                                      | 80,912       | 77,736       | 78,311           |
| Hong Kong                                   | 27,066       | 26,739       | 27,586           |
| Rest of Asia-Pacific                        | 81,031       | 63,299       | 72,265           |
| North America1                              | 56,693       | 54,884       | 55,642           |
| Latin America1                              | 66,875       | 55,241       | 64,900           |

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|                |                |                |
|----------------|----------------|----------------|
| <u>312,577</u> | <u>277,899</u> | <u>298,704</u> |
|----------------|----------------|----------------|

- In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.*
- In the first half of 2006, a charge of US\$135 million was recognised arising from the waiver of the TSR-related performance condition in respect of the 2003 awards under the HSBC Holdings Group Share Option Plan ( the Plan ). As explained in the Annual Report and Accounts 2005, in light of the impressive and sustained performance and shareholder returns over the three years covered by the 2003 awards, the Group Remuneration Committee exercised its discretion, as permitted within the Plan, to waive the TSR performance condition. Under both IFRSs and US GAAP this is treated as a modification which requires an additional accounting charge: this is a non-cash item.*

Operating expenses of US\$18,611 million were 15 per cent higher than in the first half of 2006. On an underlying basis, cost growth was 10 per cent, 5 percentage points less than the increase in net operating income before loan impairment charges.

The principal drivers of underlying cost growth were as follows:

- higher staff costs reflected increased headcount, primarily in Latin America and the Rest of Asia-Pacific region in support of business growth, and higher performance-related pay, particularly in CIBM and Private Banking, in line with strong operating income growth;
- administrative expenses increased as a result of marketing and IT expenditure to enhance brand awareness, support sales activities and promote direct banking capabilities across all regions. The emphasis on direct channels resulted in a significant increase in internet-based transactions, contributing to efficiencies that mitigated the increased cost of processing higher volumes; and
- various initiatives undertaken to support business expansion continued to augment infrastructure costs. In the UK, major costs were incurred to refurbish the branch network, improve and increase the number of self-service

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HSBC HOLDINGS PLC

**Financial Review** (continued)

machines and extend opening hours in certain branches. In the US, Mexico, Turkey and parts of the Asia-Pacific region, higher costs reflected the expansion of the retail business through branch openings and expansion of ATM networks and further development of the commercial banking operations.

## Cost efficiency ratios

HSBC's cost efficiency ratio improved from 50 per cent to 48 per cent. Significant productivity improvements in Hong Kong and the Rest of Asia-Pacific region were largely offset by a weakening cost efficiency ratio in Europe, where expenses grew at a faster rate than revenues, primarily due to the cost of overdraft fee refunds and investments made to enhance channel capacity and drive business expansion across the region.

|                                    | Half-year to         |                      |                             |
|------------------------------------|----------------------|----------------------|-----------------------------|
|                                    | 30 June<br>2007<br>% | 30 June<br>2006<br>% | 31<br>December<br>2006<br>% |
| <b>HSBC</b>                        | <b>48.3</b>          | 50.1                 | 52.5                        |
| <b>Personal Financial Services</b> | <b>50.0</b>          | 49.0                 | 50.4                        |
| Europe                             | 65.4                 | 60.2                 | 58.3                        |
| Hong Kong                          | 27.6                 | 31.1                 | 33.2                        |
| Rest of Asia-Pacific               | 68.9                 | 68.6                 | 73.1                        |
| North America <sup>1</sup>         | 41.8                 | 41.5                 | 43.0                        |
| Latin America <sup>1</sup>         | 61.9                 | 64.7                 | 66.4                        |
| <b>Commercial Banking</b>          | <b>44.2</b>          | 44.5                 | 43.1                        |
| Europe                             | 48.1                 | 48.0                 | 45.6                        |
| Hong Kong                          | 24.5                 | 27.1                 | 25.3                        |
| Rest of Asia-Pacific               | 39.3                 | 40.8                 | 43.9                        |
| North America <sup>1</sup>         | 46.4                 | 45.4                 | 44.5                        |
| Latin America <sup>1</sup>         | 55.1                 | 56.2                 | 55.6                        |

<sup>1</sup> In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

**Share of profit in associates and joint ventures**

|  | Half-year to |   |              |   |                  |   |
|--|--------------|---|--------------|---|------------------|---|
|  | 30 June 2007 |   | 30 June 2006 |   | 31 December 2006 |   |
|  | US\$m        | % | US\$m        | % | US\$m            | % |
|  |              |   |              |   |                  |   |

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**By geographical region**

|                            |            |              |      |        |     |       |
|----------------------------|------------|--------------|------|--------|-----|-------|
| Europe                     | <b>88</b>  | <b>14.1</b>  | (66) | (18.3) | (6) | (1.2) |
| Hong Kong                  | <b>13</b>  | <b>2.1</b>   | 10   | 2.8    | 9   | 1.8   |
| Rest of Asia-Pacific       | <b>507</b> | <b>81.4</b>  | 386  | 106.9  | 479 | 98.8  |
| North America <sup>1</sup> | <b>10</b>  | <b>1.6</b>   | 31   | 8.6    | (1) | (0.2) |
| Latin America <sup>1</sup> | <b>5</b>   | <b>0.8</b>   |      |        | 4   | 0.8   |
|                            | <b>623</b> | <b>100.0</b> | 361  | 100.0  | 485 | 100.0 |

Half-year to

|  | <b>30 June<br/>2007<br/>US\$m</b> | 30 June<br>2006<br>US\$m | 31<br>December<br>2006<br>US\$m |
|--|-----------------------------------|--------------------------|---------------------------------|
| Share of profit in:                              |                                   |                          |                                 |
| associates                                       | <b>607</b>                        | 357                      | 466                             |
| joint ventures                                   | <b>16</b>                         | 4                        | 19                              |
| Share of profit in associates and joint ventures | <b>623</b>                        | 361                      | 485                             |

<sup>1</sup> In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

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Income from associates and joint ventures was US\$623 million, an increase of 73 per cent compared with the first half of 2006, and 77 per cent on an underlying basis.

The commentary that follows is on an underlying basis.

Improved contributions from Bank of Communications, Industrial Bank and Ping An Insurance were partly offset by lower income from The Saudi British Bank. In Europe, share of profit in associates and joint ventures improved significantly, due to the non-recurrence of an impairment charge on a private equity investment held by an associate in the first half of 2006.

HSBC's share of income from the Bank of Communications rose significantly as a result of balance sheet growth, improved credit control and improvements in cost efficiency.

Income from Ping An Insurance also rose as a result of continued success in the core insurance business, strong performance in stock markets and successful diversification into banking.

HSBC's share of profits from The Saudi British Bank decreased 30 per cent as a result of reduced activity following a correction in the Saudi stock market in 2006, and considerable market volatility in the first half of 2007 which constrained investor appetite for equities.

**Asset deployment**

|                                 | At 30 June 2007  |              | At 30 June 2006  |              | At 31 December 2006 |              |
|---------------------------------|------------------|--------------|------------------|--------------|---------------------|--------------|
|                                 | US\$m            | %            | US\$m            | %            | US\$m               | %            |
| Loans and advances to customers | 928,101          | 43.2         | 814,209          | 46.8         | 868,133             | 46.6         |
| Loans and advances to banks     | 214,645          | 10.0         | 162,482          | 9.3          | 185,205             | 10.0         |
| Trading assets                  | 424,645          | 19.7         | 299,295          | 17.2         | 328,147             | 17.6         |
| Financial investments           | 233,001          | 10.8         | 192,334          | 11.1         | 204,806             | 11.0         |
| Derivatives                     | 149,181          | 6.9          | 104,665          | 6.1          | 103,702             | 5.6          |
| Goodwill and intangible assets  | 38,445           | 1.8          | 34,544           | 2.0          | 37,335              | 2.0          |
| Other                           | 162,423          | 7.6          | 130,609          | 7.5          | 133,430             | 7.2          |
|                                 | <b>2,150,441</b> | <b>100.0</b> | <b>1,738,138</b> | <b>100.0</b> | <b>1,860,758</b>    | <b>100.0</b> |

Loans and advances to customers include:

|                     |        |        |        |
|---------------------|--------|--------|--------|
| reverse repos       | 38,023 | 15,038 | 18,755 |
| settlement accounts | 3,948  | 8,094  | 3,254  |

Loans and advances to banks include:

|                     |        |        |        |
|---------------------|--------|--------|--------|
| reverse repos       | 49,990 | 37,101 | 45,019 |
| settlement accounts | 3,769  | 6,691  | 2,028  |

HSBC's total assets at 30 June 2007 were US\$2,150 billion, an increase of US\$289 billion or 16 per cent since 31 December 2006. CIBM was the primary driver of the increase in trading assets and derivatives. An expansion of financing-focused client business resulted in a 29 per cent increase in trading assets, while interest rate movements, a relative increase in volatility and higher volume drove a 44 per cent rise in derivatives. Acquisitions added US\$21 billion to total assets, which grew by 13 per cent on an underlying basis.

The commentary that follows is on an underlying basis.

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At 30 June 2007, HSBC's balance sheet remained highly liquid. The proportion of assets deployed in loans and advances to customers fell to 43 per cent, primarily due to significantly higher holdings of derivative and trading assets which, at US\$574 billion, accounted for 27 per cent of assets

at 30 June 2007, 4 percentage points higher than at 31 December 2006.

Loans and advances to customers increased by 5 per cent, half the rate of growth at the same point in 2006. This reflected the tightening of HSBC's personal lending criteria in its two largest personal credit markets, North America and the UK, in response to weakening credit quality in certain market segments. Emerging market credit expanded as these economies grew and HSBC improved its capacity to capture lending opportunities. HSBC's residential mortgage exposure declined marginally, with moderate growth in most of the regions in which HSBC operates, offset by a contraction in lending in North America as a result of actions taken to address exposure to the weakness seen in the sub-prime market. Personal lending, excluding mortgages, was 4 per cent higher, driven by strong growth in credit card lending in Hong Kong and increased appetite for credit in the emerging markets

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HSBC HOLDINGS PLC

## Financial Review (continued)

of Latin America and the Rest of Asia-Pacific. In Europe, growth in lending to Private Banking clients and personal lending in France and Turkey was partially offset by reduced balances in the UK as HSBC took steps to mitigate the impact of sustained high levels of personal bankruptcies and IVAs.

### Trading assets and financial investments

Trading assets principally consist of debt and equity instruments acquired for the purpose of market making or to benefit from short-term price movements. Securities classified as held for trading are carried on the balance sheet at fair value with movements in fair value recorded in the income statement.

Trading assets of US\$425 billion at 30 June 2007 were 29 per cent higher than at 31 December 2006, following the strategic decision to expand the collateralised lending business in Europe. Holdings in debt securities rose due to increased trading activity and growth in the structured notes business, while a rise in equity securities was driven by an expansion in the equity swaps franchise.

Financial investments include debt and equity instruments that are classified as available for sale or, to a small extent, held to maturity. The available-for-sale investments represent a core element of the Group's liquidity and may be disposed of either to manage that liquidity or in response to investment opportunities arising from favourable movements in economic indicators, such as interest rates, foreign exchange rates and equity prices.

Excluding the effect of acquisitions, largely Erisa, financial investments were 12 per cent higher than those reported at 31 December 2006. Higher holdings of debt securities were due to the deployment of increased commercial surplus,

particularly in the emerging market regions where HSBC's operations continued to expand.

Net unrealised gains in the valuation of equities amounted to US\$2,985 million.

### Funds under management

Funds under management at 30 June 2007 were US\$787 billion, an increase of US\$92 billion, or 13 per cent, compared with 31 December 2006. The increase was 12 per cent on an underlying basis. Both Group Investment Businesses and Private Banking delivered strong investment performance with significant net new money raised, primarily by Private Banking.

At 30 June 2007, Group Investment Businesses managed US\$343 billion of assets, a rise of 5 per cent compared with 31 December 2006, with steady investment performance.

Private Banking attracted net new money of US\$11 billion, reflecting the strength of its product range which, together with strong investment performance, contributed to an 18 per cent increase in funds under management to US\$274 billion at 30 June 2007.

Other funds under management, of which the main constituent was a corporate trust business in Asia, were 26 per cent higher than at 31 December 2006 at US\$168 billion.

Client assets, which provide an indicator of overall Private Banking volumes and include funds under management, cash deposits and certain on-balance sheet trust assets, rose by 11 per cent compared with 31 December 2006 to reach US\$370 billion. Further details of this movement are presented in the Private Banking business highlights on page 17.





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|  | Half-year to              |                           |                               |
|--|---------------------------|---------------------------|-------------------------------|
|  | 30 June<br>2007<br>US\$bn | 30 June<br>2006<br>US\$bn | 31 December<br>2006<br>US\$bn |
| <b>Funds under management</b>          |                           |                           |                               |
| At beginning of period                 | 695                       | 561                       | 615                           |
| Net new money                          | 15                        | 26                        | 18                            |
| Value change                           | 36                        | 15                        | 42                            |
| Exchange and other                     | 41                        | 13                        | 20                            |
|  | <hr/>                     | <hr/>                     | <hr/>                         |
| At end of period                       | 787                       | 615                       | 695                           |
|  | <hr/>                     | <hr/>                     | <hr/>                         |
| <b>Funds by management by business</b> |                           |                           |                               |
| Group Investment Businesses            | 343                       | 294                       | 328                           |
| Private Banking                        | 274                       | 213                       | 232                           |
| Affiliates                             | 2                         | 2                         | 2                             |
| Other                                  | 168                       | 106                       | 133                           |
|  | <hr/>                     | <hr/>                     | <hr/>                         |
|  | 787                       | 615                       | 695                           |
|  | <hr/>                     | <hr/>                     | <hr/>                         |

### Assets held in custody and under administration

Custody is the safekeeping and servicing of securities and other financial assets on behalf of clients. At 30 June 2007, assets held by HSBC as custodian amounted to US\$5,455 billion, 19 per cent higher than the US\$4,572 billion held at 31 December 2006. At constant exchange rates, growth was 18 per cent.

Administration includes the provision of various support functions, including valuations of portfolios of securities and other financial assets on behalf of clients. At 30 June 2007, the value of assets held under administration by the Group amounted to US\$1,275 billion, 11 per cent higher than the US\$1,150 billion held at 31 December 2006. At constant exchange rates, growth was 8 per cent.

### Economic profit

HSBC's internal performance measures include economic profit, a calculation which compares the return on financial capital invested in HSBC by its shareholders with the cost of that capital. HSBC prices its cost of capital internally and the difference between that cost and post-tax profit attributable to ordinary shareholders represents the amount of economic profit generated. Economic profit is used

by management as a means of deciding where to allocate resources so that they will be most productive.

In order to concentrate on external factors rather than measurement bases, HSBC emphasises the trend in economic profit rather than absolute amounts within business units. In light of the current levels of world interest rates, and taking into account its geographical and customer group diversification, HSBC believes that its true cost of capital on a consolidated basis remains 10 per cent. HSBC plans to continue using this rate until the end of the current five-year strategic plan in 2008 in order to ensure consistency and comparability.

Economic profit increased by US\$1,324 million, or 36 per cent, compared with the first half of 2006. The rate of growth in profit attributable was greater than the growth in average shareholders' equity, driven by strong growth in Hong Kong and the Rest of Asia-Pacific region, including dilution gains. The benefits from these were partly offset by higher loan impairment charges in the US and UK. The increase in economic profit was also reflected in a higher return on average invested capital and, in consequence, economic spread, which increased by 120 basis points compared with the first half of 2006.



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HSBC HOLDINGS PLC

**Financial Review** (continued)

## Economic profit

|   | Half-year to   |                |                |                |                  |                |
|---|----------------|----------------|----------------|----------------|------------------|----------------|
|   | 30 June 2007   |                | 30 June 2006   |                | 31 December 2006 |                |
|   | US\$m          | % <sup>1</sup> | US\$m          | % <sup>1</sup> | US\$m            | % <sup>1</sup> |
| Average total shareholders' equity  | 114,776        |                | 97,117         |                | 104,542          |                |
| Add: Goodwill previously amortised or written off                             | 8,172          |                | 8,172          |                | 8,172            |                |
| Less: Property revaluation reserves   | (917)          |                | (1,092)        |                | (1,032)          |                |
| Reserves representing unrealised gains/(losses) on effective cash flow hedges | 215            |                | (259)          |                | 5                |                |
| Reserves representing unrealised gains on available-for-sale securities       | (2,214)        |                | (886)          |                | (1,422)          |                |
| Preference shares   | (1,405)        |                | (1,405)        |                | (1,405)          |                |
| <b>Average invested capital<sup>2</sup></b>                                   | <b>118,627</b> |                | <b>101,647</b> |                | <b>108,860</b>   |                |
| Return on invested capital <sup>3</sup>                                       | 10,850         | 18.4           | 8,684          | 17.2           | 7,015            | 12.8           |
| Benchmark cost of capital   | (5,883)        | (10.0)         | (5,041)        | (10.0)         | (5,487)          | (10.0)         |
| <b>Economic profit/spread</b>   | <b>4,967</b>   | <b>8.4</b>     | <b>3,643</b>   | <b>7.2</b>     | <b>1,528</b>     | <b>2.8</b>     |

1 Expressed as a percentage of average invested capital.

2 Average invested capital is measured as average total shareholders' equity after adding back goodwill previously written-off directly to reserves, deducting average preference shares issued by HSBC Holdings and deducting average reserves for unrealised gains/(losses) on effective cash flow hedges and available-for-sale securities. This measure reflects capital initially invested and subsequent profit.

3 Return on invested capital is based on the profit attributable to ordinary shareholders of the parent company.

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HSBC HOLDINGS PLC

**The Management of Risk**

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**Risk management**

All HSBC's activities involve, to varying degrees, the analysis, evaluation, acceptance and management of risks or combinations of risks. The most important risks are credit risk (which includes country and cross-border risk), liquidity risk, market risk, operational risk, reputational risk and insurance risk. Market risk includes foreign exchange, interest rate and equity price risks.

HSBC's risk management policies are designed to identify and analyse these risks, to set appropriate risk limits and controls, and to monitor the risks and adherence to limits by means of reliable and up-to-date administrative and information systems. HSBC regularly reviews its risk management policies and systems to reflect

changes in markets, products and emerging best practice. Individual responsibility and accountability, instilled through training, are designed to deliver a disciplined, conservative and constructive culture of risk management and control.

The Group Management Board, under authority delegated by the Board of Directors, formulates high level Group risk management policy. A separately convened Risk Management Meeting of the Group Management Board monitors risk and receives reports which allow it to review the effectiveness of HSBC's risk management policies.

The management of all HSBC's significant risks was discussed in detail in the *Annual Report and Accounts 2006*. There have been no changes since 31 December 2006 which are material to understanding the current reporting period.

The insurance businesses manage their own credit, liquidity and market risk, along with insurance risk, separately from the rest of HSBC, due to the different nature of the respective businesses.

## Credit risk management

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### Credit exposure

The balance of exposure across the Group has not changed significantly since 31 December 2006, although growth in lending to the personal sector slowed and the underlying movement in residential mortgages was negative. The proportion of total assets deployed in loans and advances to customers decreased by 3 percentage points, as the portion of total assets represented by derivatives and trading assets increased by 1 and 2 percentage points, respectively. Within loans and advances to customers, the proportion of lending to personal customers fell slightly, as did the ratio of residential mortgage lending to total personal lending, compared with 31 December 2006. Amounts due from non-bank financial institutions increased by 37 per cent, primarily as a result of higher trading volumes in Global Markets, particularly in reverse repos. Loans and advances to banks and financial investments comprised broadly the same proportion of total assets at 30 June 2007 as they did at 31 December 2006.

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HSBC HOLDINGS PLC

**The Management of Risk** (continued)

## Gross loans and advances by industry sector

|  | At<br>31 December<br>2006<br>US\$m | Constant<br>currency<br>effect<br>US\$m | Movement on<br>a constant<br>currency basis<br>US\$m | At<br>30 June<br>2007<br>US\$m |
|--|------------------------------------|---|--|--------------------------------|
| <b>Loans and advances to customers</b>             |                                    |   |  |                                |
| Personal:  |                                    |   |  |                                |
| Residential mortgages <sup>1</sup>                 | 265,337                            | 3,816                                   | (2,329)  | <b>266,824</b>                 |
| Other personal <sup>2</sup>                        | 210,809                            | 2,750                                   | 8,493  | <b>222,052</b>                 |
| <b>Total personal</b>                              | <b>476,146</b>                     | <b>6,566</b>                            | <b>6,164</b>   | <b>488,876</b>                 |
| Corporate and commercial:                          |                                    |   |  |                                |
| Commercial, industrial and international trade     | 162,109                            | 3,579                                   | 10,663   | <b>176,351</b>                 |
| Commercial real estate                             | 60,366                             | 1,327                                   | 2,645  | <b>64,338</b>                  |
| Other property-related                             | 27,165                             | 658                                     | 1,050  | <b>28,873</b>                  |
| Government   | 8,990                              | 69                                      | (1,495)  | <b>7,564</b>                   |
| Other commercial <sup>3</sup>                      | 84,477                             | 1,827                                   | 4,801  | <b>91,105</b>                  |
| <b>Total corporate and commercial</b>              | <b>343,107</b>                     | <b>7,460</b>                            | <b>17,664</b>  | <b>368,231</b>                 |
| Financial:   |                                    |   |  |                                |
| Non-bank financial institutions                    | 59,204                             | 1,041                                   | 21,124   | <b>81,369</b>                  |
| Settlement accounts                                | 3,254                              | 29                                      | 665  | <b>3,948</b>                   |
| <b>Total financial</b>                             | <b>62,458</b>                      | <b>1,070</b>                            | <b>21,789</b>  | <b>85,317</b>                  |
| <b>Total gross loans and advances to customers</b> | <b>881,711</b>                     | <b>15,096</b>                           | <b>45,617</b>  | <b>942,424</b>                 |
| <b>Loans and advances to banks</b>                 | <b>185,212</b>                     | <b>2,906</b>                            | <b>26,534</b>  | <b>214,652</b>                 |
| <b>Total gross loans and advances</b>              | <b>1,066,923</b>                   | <b>18,002</b>                           | <b>72,151</b>  | <b>1,157,076</b>               |

1 Including Hong Kong Government Home Ownership Scheme loans of US\$3,972 million at 30 June 2007.

2 Including second lien mortgages and other property-related lending.

3 Including advances in respect of agriculture, transport, energy and utilities.

The commentary below analyses, on a constant currency basis, the changes in lending noted in the table above, compared with the position at 31 December 2006. On this basis, loans and advances to personal, corporate and commercial customers grew by 3 per cent, and total gross loans and advances increased by 7 per cent.

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Geographically, total lending to personal customers was dominated by the diverse portfolios in North America (US\$229 billion), the UK (US\$130 billion) and Hong Kong (US\$44 billion). Collectively, these lending books accounted for 82 per cent of total lending to the personal sector, 2 percentage points lower than the level reported at 31 December 2006.

Residential mortgages declined marginally to US\$267 billion, representing 28 per cent of total loans and advances to customers (including the finance sector and settlement accounts) at 30 June 2007. In value terms, there was modest growth in Europe (US\$1.2 billion) and strong growth in Rest of Asia-Pacific (US\$0.9 billion), though this was more than offset by the planned contraction of the US mortgage services loan book.

In Europe, residential mortgage balances increased by 1 per cent to US\$95 billion. In the UK, mortgage lending was broadly in line with

31 December 2006, with a change in product mix in favour of fixed rate mortgages. In France, balances grew 7 per cent to US\$5 billion due to customer recruitment and strong demand for credit. In Turkey, strong growth of 10 per cent in mortgage lending was aided by the launch of a pre-approved mortgage campaign aimed at existing credit card customers.

In Hong Kong, the residential property market was boosted by a strong economy; however, the continued run-off of the Government Home Ownership Scheme and the competitive market environment led to a marginal decline in balances.

In North America, residential mortgage balances decreased by 4 per cent. In the US, the level of mortgage lending stood at US\$103 billion, a decrease of 5 per cent since 31 December 2006. Non-prime balances in the consumer lending business increased, but this was more than offset by the result of actions taken in the mortgage services business, including tightening underwriting criteria, the decision to stop purchasing mortgages from correspondent brokers, and the continuation of the strategy of the US bank to sell down the majority of its prime loans. In Canada, the continued strength of the housing market and branch expansion by the consumer finance business contributed to 3 per cent growth in the residential mortgage book to US\$17 billion.

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There was good growth in mortgage lending in many of the emerging market economies in the Rest of Asia-Pacific and Latin America regions, where balances rose by 5 per cent and 9 per cent, respectively.

Other personal lending grew by 4 per cent, to US\$222 billion, representing 24 per cent of total loans and advances to customers (including the finance sector and settlement accounts) at 30 June 2007.

In Europe, other personal lending grew modestly. Growth in lending to Private Banking clients in Switzerland and greater levels of cross-sales to credit card customers in Turkey was partially offset by reduced balances in the UK as HSBC took steps to mitigate the adverse impact of sustained high levels of personal bankruptcies and IVAs.

Promotional campaigns boosted HSBC's cards in circulation in Hong Kong, where the Group's market leadership continued, and contributed to a substantial increase in other personal lending balances.

In Rest of Asia-Pacific, other personal lending was 10 per cent higher than at 31 December 2006, driven by strong growth in credit cards in circulation in the Middle East and robust expansion in personal lending in India, following branch expansion and marketing activity.

In North America, other personal lending balances reduced by 1 percentage point from the level at 31 December 2006. This decrease occurred in the US, where second lien mortgage balances, which do not meet the accounting definition of residential mortgages, declined significantly following HSBC's decision to reduce this exposure. The reduction outweighed the results of increased marketing activity and direct mail campaigns that led to strong organic growth in credit cards and other personal lending.

Strong growth in credit card lending contributed to a 17 per cent rise in other personal lending in Latin America. In Mexico, personal lending rose following marketing campaigns and incentive offers, which contributed to increased credit card balances. In Brazil, growth in merchant relationships and the launch of a Visa credit card, together with higher levels of instalment and vehicle loans, led to increased other personal lending balances.

Loans and advances to corporate and commercial customers, at US\$368 billion, were 4 per cent higher than at 31 December 2006. Lending was primarily concentrated in Europe, where it accounted for 58 per cent of advances to this sector, more than three quarters of which were in the UK.

In Europe, corporate and commercial advances were 6 per cent higher than at 31 December 2006. In the UK, lending to the commercial, industrial and international trade segment grew by 5 per cent following strong customer recruitment and improved cross-sales. In France, lending balances were 3 per cent higher than at 31 December 2006, mainly driven by the commercial, industrial and international, and commercial real estate segments. Commercial lending balances also saw strong growth in Germany.

In Hong Kong, strong cross-border lending to manufacturers with operations in mainland China was offset by reduced lending to the commercial real estate sector. In Rest of Asia-Pacific, the commercial loan book continued to expand. HSBC incorporated locally in mainland China and this added impetus to the Group's already strong corporate and commercial offering, leading to significant growth in lending balances. In the Middle East, the addition of new relationship managers in the Business Banking Unit for small and micro businesses stimulated growth of the customer base, though this was partially offset by reduced lending to governments. In India, the extension of HSBC's Commercial Banking proposition further into the branch network aided strong customer acquisition and contributed to increased lending balances.

In North America, the continued expansion of the branch network across the US and the effects of a strong focus on generating higher volumes of business from small and mid-market customers contributed to growth in commercial lending balances despite tightening of underwriting criteria for certain small and micro business customers.

HSBC's Commercial Banking business continued to develop in Latin America and this was reflected in the expansion of the corporate and commercial loan portfolio. In Mexico, economic growth fuelled demand for credit to facilitate construction projects and this, together with sales of *Estimulo*, a packaged product targeted at small businesses, contributed to increased customer numbers and higher levels of corporate and commercial lending. In Brazil, the growth in the corporate and commercial loan book was driven by a number of factors including the granting of higher





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HSBC HOLDINGS PLC

**The Management of Risk** (continued)

facility limits for some customers, the continued success of the giro facil product, which combines loan and overdraft facilities, and increased appetite for credit from the real estate and agricultural sectors.

The following tables analyse loans by industry

sector and by the location of the principal operations of the lending subsidiary or, in the case of the operations of The Hongkong and Shanghai Banking Corporation Limited, HSBC Bank plc, HSBC Bank Middle East Limited and HSBC Bank USA N.A., by the location of the lending branch.

**Loans and advances to customers by industry sector and by geographical region**

At 30 June 2007

|  | Europe<br>US\$m | Hong<br>Kong<br>US\$m | Rest of<br>Asia-<br>Pacific<br>US\$m | North<br>America<br>US\$m | Latin<br>America<br>US\$m | Gross<br>loans and<br>advances<br>to<br>customers<br>US\$m | Gross<br>loans<br>by<br>industry<br>sector as a<br>% of total<br>gross<br>loans<br>% |
|--|-----------------|-----------------------|--------------------------------------|---------------------------|---------------------------|--|--|
| <b>Personal</b>                                |                 |                       |                                      |                           |                           |  |  |
| Residential mortgages <sup>1</sup>             | 94,792          | 28,448                | 18,958                               | 120,621                   | 4,005                     | 266,824  | 28.3   |
| Other personal                                 | 69,170          | 15,352                | 14,835                               | 108,077                   | 14,618                    | 222,052  | 23.6   |
|  | <u>163,962</u>  | <u>43,800</u>         | <u>33,793</u>                        | <u>228,698</u>            | <u>18,623</u>             | <u>488,876</u>   | <u>51.9</u>  |
| <b>Corporate and commercial</b>                |                 |                       |                                      |                           |                           |  |  |
| Commercial, industrial and international trade | 106,209         | 16,699                | 30,243                               | 11,844                    | 11,356                    | 176,351  | 18.7   |
| Commercial real estate                         | 31,706          | 11,584                | 6,788                                | 13,115                    | 1,145                     | 64,338   | 6.8  |
| Other property-related                         | 9,541           | 7,585                 | 3,767                                | 6,634                     | 1,346                     | 28,873   | 3.1  |
| Government                                     | 1,981           | 356                   | 1,076                                | 256                       | 3,895                     | 7,564  | 0.8  |
| Other commercial <sup>2</sup>                  | 64,163          | 5,341                 | 8,958                                | 8,543                     | 4,100                     | 91,105   | 9.7  |
|  | <u>213,600</u>  | <u>41,565</u>         | <u>50,832</u>                        | <u>40,392</u>             | <u>21,842</u>             | <u>368,231</u>   | <u>39.1</u>  |
| <b>Financial</b>                               |                 |                       |                                      |                           |                           |  |  |
| Non-bank financial institutions                | 52,683          | 3,671                 | 3,969                                | 19,287                    | 1,759                     | 81,369   | 8.6  |

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|  |                |               |               |                |               |                |              |
|--|----------------|---------------|---------------|----------------|---------------|----------------|--------------|
| Settlement accounts  | <u>1,506</u>   | <u>1,217</u>  | <u>520</u>    | <u>632</u>     | <u>73</u>     | <u>3,948</u>   | <u>0.4</u>   |
|  | <u>54,189</u>  | <u>4,888</u>  | <u>4,489</u>  | <u>19,919</u>  | <u>1,832</u>  | <u>85,317</u>  | <u>9.0</u>   |
| Total gross loans and advances to customers <sup>3</sup>                         | <u>431,751</u> | <u>90,253</u> | <u>89,114</u> | <u>289,009</u> | <u>42,297</u> | <u>942,424</u> | <u>100.0</u> |
| Percentage of Group loans and advances by geographical region                    | <b>45.8%</b>   | <b>9.6%</b>   | <b>9.4%</b>   | <b>30.7%</b>   | <b>4.5%</b>   | <b>100.0%</b>  |              |
| Impaired loans <sup>4</sup>  | <b>5,849</b>   | <b>467</b>    | <b>1,209</b>  | <b>5,226</b>   | <b>1,804</b>  | <b>14,555</b>  |              |
| Impaired loans as a percentage of gross loans and advances to customers          | <b>1.4%</b>    | <b>0.5%</b>   | <b>1.4%</b>   | <b>1.8%</b>    | <b>4.3%</b>   | <b>1.5%</b>    |              |
| Impairment allowances outstanding against loans and advances <sup>5</sup>        | <b>3,643</b>   | <b>335</b>    | <b>940</b>    | <b>7,714</b>   | <b>1,691</b>  | <b>14,323</b>  |              |
| Impairment allowances outstanding as a percentage of impaired loans <sup>5</sup> | <b>62.3%</b>   | <b>71.7%</b>  | <b>77.8%</b>  | <b>147.6%</b>  | <b>93.7%</b>  | <b>98.4%</b>   |              |

1 Including Hong Kong Government Home Ownership Scheme loans of US\$3,972 million.

2 Including advances in respect of agriculture, transport, energy and utilities.

3 Including credit card lending of US\$76,211 million.

4 Includes loans individually assessed as impaired and collectively assessed loans with a high likelihood of default. Impairment allowances establish a best estimate of loss arising on both these categories of loans and on the remaining book of collectively assessed loans.

5 Including collective impairment allowances on collectively assessed loans and advances.

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At 30 June 2006 (restated<sup>1</sup>)

|  | Europe<br>US\$m | Hong<br>Kong<br>US\$m | Rest of<br>Asia-<br>Pacific<br>US\$m | North<br>America<br>US\$m | Latin<br>America<br>US\$m | Gross<br>loans and<br>advances<br>to<br>customers<br>US\$m | Gross<br>loans<br>by<br>industry<br>sector as<br>a<br>% of total<br>gross<br>loans<br>% |
|--|-----------------|-----------------------|--------------------------------------|---------------------------|---------------------------|--|---|
| <b>Personal</b>  |                 |                       |                                      |                           |                           |  |   |
| Residential mortgages <sup>2</sup>   | 83,401          | 28,939                | 18,536                               | 122,555                   | 2,199                     | 255,630  | 30.9  |
| Other personal   | 60,359          | 9,644                 | 11,878                               | 102,082                   | 8,449                     | 192,412  | 23.3  |
|  | <u>143,760</u>  | <u>38,583</u>         | <u>30,414</u>                        | <u>224,637</u>            | <u>10,648</u>             | <u>448,042</u>   | <u>54.2</u>   |
| <b>Corporate and commercial</b>  |                 |                       |                                      |                           |                           |  |   |
| Commercial, industrial and international trade                                   | 91,702          | 17,841                | 23,330                               | 10,583                    | 6,739                     | 150,195  | 18.2  |
| Commercial real estate   | 24,838          | 13,313                | 5,414                                | 13,152                    | 419                       | 57,136   | 6.9   |
| Other property-related   | 8,583           | 6,151                 | 3,112                                | 5,481                     | 729                       | 24,056   | 2.9   |
| Government   | 1,702           | 418                   | 1,846                                | 202                       | 3,755                     | 7,923  | 1.0   |
| Other commercial <sup>3</sup>  | 50,429          | 6,349                 | 8,593                                | 8,805                     | 2,418                     | 76,594   | 9.3   |
|  | <u>177,254</u>  | <u>44,072</u>         | <u>42,295</u>                        | <u>38,223</u>             | <u>14,060</u>             | <u>315,904</u>   | <u>38.3</u>   |
| <b>Financial</b>   |                 |                       |                                      |                           |                           |  |   |
| Non-bank financial institutions  | 36,933          | 2,493                 | 2,436                                | 10,280                    | 1,407                     | 53,549   | 6.5   |
| Settlement accounts  | 4,965           | 1,397                 | 604                                  | 980                       | 149                       | 8,095  | 1.0   |
|  | <u>41,898</u>   | <u>3,890</u>          | <u>3,040</u>                         | <u>11,260</u>             | <u>1,556</u>              | <u>61,644</u>  | <u>7.5</u>  |
| <b>Total gross loans and advances to customers<sup>4</sup></b>                   | <u>362,912</u>  | <u>86,545</u>         | <u>75,749</u>                        | <u>274,120</u>            | <u>26,264</u>             | <u>825,590</u>   | <u>100.0</u>  |
| <b>Percentage of Group loans and advances by geographical region</b>             |                 |                       |                                      |                           |                           |  |   |
| Impaired loans   | 43.9%           | 10.5%                 | 9.2%                                 | 33.2%                     | 3.2%                      | 100.0%   |   |
| Impaired loans as a percentage of gross loans and advances to customers          | 5,767           | 504                   | 1,041                                | 3,638                     | 1,346                     | 12,296   |   |
| Impairment allowances outstanding against loans and advances <sup>5</sup>        | 1.6%            | 0.6%                  | 1.4%                                 | 1.3%                      | 5.1%                      | 1.5%   |   |
| Impairment allowances outstanding as a percentage of impaired loans <sup>5</sup> | 3,513           | 391                   | 910                                  | 5,249                     | 1,318                     | 11,381   |   |
|  | 60.9%           | 77.6%                 | 87.4%                                | 144.3%                    | 97.9%                     | 92.6%  |   |

1 In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

2 Including Hong Kong Government Home Ownership Scheme loans of US\$4,360 million.

3 Including advances in respect of agriculture, transport, energy and utilities.

4 Including credit card lending of US\$65,953 million.

5 Including collective impairment allowances on collectively assessed loans and advances.



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HSBC HOLDINGS PLC

**The Management of Risk** (continued)**Loans and advances to customers by industry sector and by geographical region** (continued)

At 31 December 2006

|   | Europe<br>US\$m | Hong<br>Kong<br>US\$m | Rest of<br>Asia-<br>Pacific<br>US\$m | North<br>America<br>US\$m | Latin<br>America<br>US\$m | Gross<br>loans and<br>advances<br>to<br>customers<br>US\$m | Gross<br>loans<br>by industry<br>sector as a<br>% of total<br>gross loans<br>% |
|---|-----------------|-----------------------|--------------------------------------|---------------------------|---------------------------|--|--|
| <b>Personal</b>   |                 |                       |                                      |                           |                           |  |  |
| Residential mortgages <sup>1</sup>  | 91,534          | 28,743                | 17,478                               | 123,955                   | 3,627                     | 265,337  | 30.1   |
| Other personal  | 67,214          | 10,396                | 13,275                               | 108,256                   | 11,668                    | 210,809  | 23.9   |
|   | <u>158,748</u>  | <u>39,139</u>         | <u>30,753</u>                        | <u>232,211</u>            | <u>15,295</u>             | <u>476,146</u>   | <u>54.0</u>  |
| <b>Corporate and commercial</b>   |                 |                       |                                      |                           |                           |  |  |
| Commercial, industrial and<br>international trade                                   | 99,027          | 16,845                | 25,196                               | 11,004                    | 10,037                    | 162,109  | 18.4   |
| Commercial real estate  | 28,655          | 12,481                | 5,502                                | 12,782                    | 946                       | 60,366   | 6.8  |
| Other property-related  | 9,616           | 6,923                 | 3,491                                | 5,931                     | 1,204                     | 27,165   | 3.1  |
| Government  | 2,360           | 551                   | 1,916                                | 220                       | 3,943                     | 8,990  | 1.0  |
| Other commercial <sup>2</sup>   | 56,650          | 5,553                 | 8,468                                | 9,736                     | 4,070                     | 84,477   | 9.6  |
|   | <u>196,308</u>  | <u>42,353</u>         | <u>44,573</u>                        | <u>39,673</u>             | <u>20,200</u>             | <u>343,107</u>   | <u>38.9</u>  |
| <b>Financial</b>  |                 |                       |                                      |                           |                           |  |  |
| Non-bank financial institutions   | 40,055          | 2,332                 | 2,926                                | 12,258                    | 1,633                     | 59,204   | 6.7  |
| Settlement accounts   | 1,064           | 823                   | 223                                  | 1,092                     | 52                        | 3,254  | 0.4  |
|   | <u>41,119</u>   | <u>3,155</u>          | <u>3,149</u>                         | <u>13,350</u>             | <u>1,685</u>              | <u>62,458</u>  | <u>7.1</u>   |
| <b>Total gross loans and advances to<br/>customers<sup>3</sup></b>                  | <u>396,175</u>  | <u>84,647</u>         | <u>78,475</u>                        | <u>285,234</u>            | <u>37,180</u>             | <u>881,711</u>   | <u>100.0</u>   |
| <b>Percentage of Group loans and<br/>advances by geographical region</b>            | 44.9%           | 9.6%                  | 8.9%                                 | 32.4%                     | 4.2%                      | 100.0%   |  |
| <b>Impaired loans</b>   | 5,847           | 454                   | 1,184                                | 4,822                     | 1,478                     | 13,785   |  |
| <b>Impaired loans as a percentage of gross<br/>loans and advances to customers</b>  | 1.5%            | 0.5%                  | 1.5%                                 | 1.7%                      | 4.0%                      | 1.6%   |  |
| <b>Impairment allowances outstanding<br/>against loans and advances<sup>4</sup></b> | 3,676           | 365                   | 901                                  | 7,247                     | 1,389                     | 13,578   |  |
|   | 62.9%           | 80.4%                 | 76.1%                                | 150.3%                    | 94.0%                     | 98.5%  |  |

Impairment allowances outstanding as a percentage of impaired loans<sup>4</sup>

1 Including Hong Kong Government Home Ownership Scheme loans of US\$4,078 million.

2 Including advances in respect of agriculture, transport, energy and utilities.

3 Including credit card lending of US\$74,518 million.

4 Including collective impairment allowances on collectively assessed loans and advances.

Included in personal lending in North America are the following balances relating to the US:

|                                     | At             | At             | At             |
|-------------------------------------|----------------|----------------|----------------|
|                                     | 30 June        | 30 June        | 31             |
|                                     | 2007           | 2006           | December       |
|                                     | US\$m          | US\$m          | 2006           |
|                                     |                |                | US\$m          |
| Residential mortgages HSBC Bank USA | 29,725         | 33,762         | 31,589         |
| Residential mortgages HSBC Finance  | 72,838         | 72,675         | 75,903         |
| Motor vehicle finance               | 13,205         | 13,012         | 13,146         |
| MasterCard and Visa credit cards    | 30,393         | 26,598         | 29,269         |
| Private label cards                 | 15,942         | 14,766         | 16,645         |
| Other personal lending              | 39,257         | 39,926         | 41,214         |
|                                     | <u>201,360</u> | <u>200,739</u> | <u>207,766</u> |

[Back to Contents](#)**Gross loans and advances to customers by country within Rest of Asia-Pacific and Latin America**

At 30 June 2007

|                                      | Residential<br>mortgages<br>US\$m | Other<br>personal<br>US\$m | Property-<br>related<br>US\$m | Commercial,<br>international<br>trade and<br>other<br>US\$m | Total<br>US\$m |
|--------------------------------------|-----------------------------------|----------------------------|-------------------------------|---|----------------|
| Australia                            | 4,114                             | 846                        | 1,896                         | 3,009   | 9,865          |
| India                                | 1,538                             | 1,429                      | 331                           | 2,987   | 6,285          |
| Indonesia                            | 21                                | 405                        | 3                             | 928   | 1,357          |
| Japan                                | 17                                | 125                        | 536                           | 2,906   | 3,584          |
| Mainland China                       | 382                               | 7                          | 1,647                         | 4,804   | 6,840          |
| Malaysia                             | 2,441                             | 1,343                      | 649                           | 3,687   | 8,120          |
| Middle East (excluding Saudi Arabia) | 678                               | 3,702                      | 2,072                         | 10,863  | 17,315         |
| Egypt                                |                                   | 154                        | 73                            | 1,014   | 1,241          |
| United Arab Emirates                 | 577                               | 2,385                      | 1,446                         | 6,610   | 11,018         |
| Other Middle East                    | 101                               | 1,163                      | 553                           | 3,239   | 5,056          |
| Singapore                            | 3,347                             | 3,217                      | 1,346                         | 2,889   | 10,799         |
| South Korea                          | 2,769                             | 888                        | 49                            | 2,763   | 6,469          |
| Taiwan                               | 2,174                             | 767                        | 16                            | 1,020   | 3,977          |
| Other                                | 1,477                             | 2,106                      | 2,010                         | 8,910   | 14,503         |
| <b>Total of Rest of Asia-Pacific</b> | <b>18,958</b>                     | <b>14,835</b>              | <b>10,555</b>                 | <b>44,766</b>   | <b>89,114</b>  |
| Argentina                            | 54                                | 498                        | 74                            | 1,524   | 2,150          |
| Brazil                               | 253                               | 8,204                      | 308                           | 6,234   | 14,999         |
| Mexico                               | 2,031                             | 4,057                      | 1,040                         | 9,504   | 16,632         |
| Other                                | 1,667                             | 1,859                      | 1,069                         | 3,921   | 8,516          |
| <b>Total of Latin America</b>        | <b>4,005</b>                      | <b>14,618</b>              | <b>2,491</b>                  | <b>21,183</b>   | <b>42,297</b>  |

At 30 June 2006 (restated<sup>1</sup>)

|                                      | Residential<br>mortgages<br>US\$m | Other<br>personal<br>US\$m | Property-<br>related<br>US\$m | Commercial,<br>international<br>trade and<br>other<br>US\$m | Total<br>US\$m |
|--------------------------------------|-----------------------------------|----------------------------|-------------------------------|---|----------------|
| Australia                            | 4,714                             | 442                        | 1,647                         | 3,033   | 9,836          |
| India                                | 1,219                             | 734                        | 196                           | 2,040   | 4,189          |
| Indonesia                            | 15                                | 361                        | 2                             | 1,007   | 1,385          |
| Japan                                | 15                                | 148                        | 719                           | 2,715   | 3,597          |
| Mainland China                       | 372                               | 12                         | 1,166                         | 3,986   | 5,536          |
| Malaysia                             | 2,357                             | 1,050                      | 526                           | 3,326   | 7,259          |
| Middle East (excluding Saudi Arabia) | 301                               | 2,619                      | 1,542                         | 10,373  | 14,835         |



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|                               |                   |                   |                   |                   |                   |
|-------------------------------|-------------------|-------------------|-------------------|-------------------|-------------------|
| Egypt                         |                   | 107               | 42                | 859               | 1,008             |
| United Arab Emirates          | 216               | 1,591             | 1,270             | 6,438             | 9,515             |
| Other Middle East             | 85                | 921               | 230               | 3,076             | 4,312             |
| Singapore                     | 3,137             | 3,340             | 1,460             | 2,217             | 10,154            |
| South Korea                   | 2,673             | 681               | 17                | 2,263             | 5,634             |
| Taiwan                        | 2,241             | 1,014             | 17                | 851               | 4,123             |
| Other                         | 1,492             | 1,477             | 1,234             | 4,998             | 9,201             |
|                               | <u>          </u> | <u>          </u> | <u>          </u> | <u>          </u> | <u>          </u> |
| Total of Rest of Asia-Pacific | 18,536            | 11,878            | 8,526             | 36,809            | 75,749            |
|                               | <u>          </u> | <u>          </u> | <u>          </u> | <u>          </u> | <u>          </u> |
| Argentina                     | 68                | 187               | 42                | 1,473             | 1,770             |
| Brazil                        | 200               | 5,494             | 242               | 4,485             | 10,421            |
| Mexico                        | 1,458             | 2,602             | 640               | 7,748             | 12,448            |
| Other                         | 473               | 166               | 224               | 762               | 1,625             |
|                               | <u>          </u> | <u>          </u> | <u>          </u> | <u>          </u> | <u>          </u> |
| Total of Latin America        | 2,199             | 8,449             | 1,148             | 14,468            | 26,264            |
|                               | <u>          </u> | <u>          </u> | <u>          </u> | <u>          </u> | <u>          </u> |

1 *In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.*

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HSBC HOLDINGS PLC

**The Management of Risk** (continued)**Gross loans and advances to customers by country within Rest of Asia-Pacific and Latin America** (continued)

At 31 December 2006

|                                      | Residential<br>mortgages<br>US\$m | Other<br>personal<br>US\$m | Property-<br>related<br>US\$m | Commercial,<br>international<br>trade and<br>other<br>US\$m | Total<br>US\$m |
|--------------------------------------|-----------------------------------|----------------------------|-------------------------------|---|----------------|
| Australia                            | 3,637                             | 586                        | 1,615                         | 2,951   | 8,789          |
| India                                | 1,338                             | 1,067                      | 203                           | 2,363   | 4,971          |
| Indonesia                            | 17                                | 371                        | 2                             | 1,014   | 1,404          |
| Japan                                | 18                                | 131                        | 648                           | 2,601   | 3,398          |
| Mainland China                       | 377                               | 9                          | 1,504                         | 4,226   | 6,116          |
| Malaysia                             | 2,456                             | 1,277                      | 589                           | 3,537   | 7,859          |
| Middle East (excluding Saudi Arabia) | 434                               | 3,134                      | 1,733                         | 10,595  | 15,896         |
| Egypt                                |                                   | 125                        | 60                            | 825   | 1,010          |
| United Arab Emirates                 | 331                               | 1,977                      | 1,308                         | 6,602   | 10,218         |
| Other Middle East                    | 103                               | 1,032                      | 365                           | 3,168   | 4,668          |
| Singapore                            | 3,090                             | 3,225                      | 1,286                         | 2,052   | 9,653          |
| South Korea                          | 2,708                             | 862                        | 45                            | 2,655   | 6,270          |
| Taiwan                               | 2,273                             | 881                        | 15                            | 970   | 4,139          |
| Other                                | 1,130                             | 1,732                      | 1,353                         | 5,765   | 9,980          |
| <b>Total of Rest of Asia-Pacific</b> | <b>17,478</b>                     | <b>13,275</b>              | <b>8,993</b>                  | <b>38,729</b>   | <b>78,475</b>  |
| Argentina                            | 22                                | 314                        | 52                            | 1,625   | 2,013          |
| Brazil                               | 211                               | 6,579                      | 251                           | 5,212   | 12,253         |
| Mexico                               | 1,801                             | 3,353                      | 959                           | 8,648   | 14,761         |
| Other                                | 1,593                             | 1,422                      | 888                           | 4,250   | 8,153          |
| <b>Total of Latin America</b>        | <b>3,627</b>                      | <b>11,668</b>              | <b>2,150</b>                  | <b>19,735</b>   | <b>37,180</b>  |

**Loans and advances to banks by geographical region**

|  | Hong<br>Kong<br>US\$m | Rest of<br>Asia-<br>Pacific<br>US\$m | North<br>America<br>US\$m | Latin<br>America<br>US\$m | Gross<br>loans and<br>advances<br>to banks<br>US\$m | Impairment<br>allowances<br>US\$m |
|--|-----------------------|--------------------------------------|---------------------------|---------------------------|---|-----------------------------------|
|--|-----------------------|--------------------------------------|---------------------------|---------------------------|---|-----------------------------------|

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|                        |               |               |               |               |               |                |            |
|------------------------|---------------|---------------|---------------|---------------|---------------|----------------|------------|
| <b>At 30 June 2007</b> | <b>79,824</b> | <b>68,162</b> | <b>34,678</b> | <b>18,643</b> | <b>13,345</b> | <b>214,652</b> | <b>(7)</b> |
| At 30 June 2006        | 64,570        | 45,288        | 26,460        | 16,754        | 9,418         | 162,490        | (8)        |
| At 31 December 2006    | 76,837        | 50,359        | 27,517        | 17,865        | 12,634        | 185,212        | (7)        |

1 *In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.*

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Financial assets net exposure to credit risk

HSBC has legally enforceable rights to offset certain financial assets with financial liabilities. In normal circumstances there would be no intention of settling net, nor of realising the financial assets and settling

the financial liabilities simultaneously. Consequently, the financial assets are not offset against the respective financial liabilities for reporting purposes. However, the exposure to credit risk relating to the respective financial assets is mitigated as follows:

|   | At 30 June 2007             |                 |  | At 30 June 2006             |                 |  | At 31 December 2006         |                 |  |
|---|-----------------------------|-----------------|--|-----------------------------|-----------------|--|-----------------------------|-----------------|--|
|   | Carrying<br>amount<br>US\$m | Offset<br>US\$m | Net<br>exposure<br>to credit<br>risk <sup>1</sup><br>US\$m | Carrying<br>amount<br>US\$m | Offset<br>US\$m | Net<br>exposure<br>to credit<br>risk <sup>1</sup><br>US\$m | Carrying<br>amount<br>US\$m | Offset<br>US\$m | Net<br>exposure<br>to credit<br>risk <sup>1</sup><br>US\$m |
| Loans and advances held at amortised cost |                             |                 |  |                             |                 |  |                             |                 |  |
| Loans and advances to customers           | 928,101                     | (82,213)        | 845,888  | 814,209                     | (61,802)        | 752,407  | 868,133                     | (68,076)        | 800,057  |
| Loans and advances to banks               | 214,645                     | (443)           | 214,202  | 162,482                     | (1)             | 162,481  | 185,205                     | (455)           | 184,750  |
|   | <b>1,142,746</b>            | <b>(82,656)</b> | <b>1,060,090</b>   | <b>976,691</b>              | <b>(61,803)</b> | <b>914,888</b>   | <b>1,053,338</b>            | <b>(68,531)</b> | <b>984,807</b>   |
| Trading assets                            |                             |                 |  |                             |                 |  |                             |                 |  |
| Treasury and other eligible bills         | 10,407                      |                 | 10,407   | 12,005                      |                 | 12,005   | 21,759                      | (16)            | 21,743   |
| Debt securities                           | 176,636                     | (830)           | 175,806  | 146,374                     | (232)           | 146,142  | 155,447                     | (1,036)         | 154,411  |
| Loans and advances to banks               | 95,710                      | (12)            | 95,698   | 47,416                      |                 | 47,416   | 52,006                      |                 | 52,006   |
| Loans and advances to customers           | 106,405                     | (5,934)         | 100,471  | 69,788                      | (5,661)         | 64,127   | 71,786                      | (7,186)         | 64,600   |
|   | <b>389,158</b>              | <b>(6,776)</b>  | <b>382,382</b>   | <b>275,583</b>              | <b>(5,893)</b>  | <b>269,690</b>   | <b>300,998</b>              | <b>(8,238)</b>  | <b>292,760</b>   |
| Financial assets designated at fair value |                             |                 |  |                             |                 |  |                             |                 |  |

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|                                   |                  |                  |                  |           |           |           |           |           |           |
|-----------------------------------|------------------|------------------|------------------|-----------|-----------|-----------|-----------|-----------|-----------|
| Treasury and other eligible bills | 206              |                  | 206              | 80        |           | 80        | 133       |           | 133       |
| Debt securities                   | 15,832           |                  | 15,832           | 5,934     | (465)     | 5,469     | 9,449     |           | 9,449     |
| Loans and advances to banks       | 356              |                  | 356              | 212       |           | 212       | 236       |           | 236       |
| Loans and advances to customers   | 136              |                  | 136              | 389       |           | 389       | 153       |           | 153       |
|                                   | <b>16,530</b>    |                  | <b>16,530</b>    | 6,615     | (465)     | 6,150     | 9,971     |           | 9,971     |
| Derivatives                       | 149,181          | (109,910)        | 39,271           | 104,665   | (65,993)  | 38,672    | 103,702   | (62,741)  | 40,961    |
| Financial investments             |                  |                  |                  |           |           |           |           |           |           |
| Treasury and other similar bills  | 26,077           |                  | 26,077           | 23,769    |           | 23,769    | 25,313    | (30)      | 25,283    |
| Debt securities                   | 197,621          |                  | 197,621          | 161,583   |           | 161,583   | 171,196   | (1)       | 171,195   |
|                                   | <b>223,698</b>   |                  | <b>223,698</b>   | 185,352   |           | 185,352   | 196,509   | (31)      | 196,478   |
| Other assets                      |                  |                  |                  |           |           |           |           |           |           |
| Endorsements and acceptances      | 10,911           | (209)            | 10,702           | 8,706     | (9)       | 8,697     | 9,577     | (187)     | 9,390     |
|                                   | <b>1,932,224</b> | <b>(199,551)</b> | <b>1,732,673</b> | 1,557,612 | (134,163) | 1,423,449 | 1,674,095 | (139,728) | 1,534,367 |

1 Excluding the value of any collateral or security held.

#### Areas of special interest

##### Mortgage lending products

HSBC underwrites first lien residential mortgages and loans secured by second lien mortgages which are reported within other personal lending in the market sector analysis. In addition to capital or principal repayment mortgages that may be subject to either fixed or variable interest rates, HSBC responds to customer needs by periodically testing and underwriting mortgage products designed to meet demand for flexible house purchase loans.

Interest only mortgages, including endowment mortgages, which are more prevalent in the UK than elsewhere in the Group, allow customers to pay only the interest that accrues on the loan, with the principal sum repaid at a later stage. In most cases, customers contribute to an endowment or other investment policy that should, on maturity, provide sufficient capital to repay the principal amount. Alternatively, customers may repay the principal of their loans from the proceeds of sale of the



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property on which the loan is secured, or from other repayment sources.

Affordability mortgages include all products for which the customer's monthly payments are maintained at a low or fixed level in early periods using discounted or fixed interest rates, or an interest-only introductory period, before resetting to a higher variable rate or a capital repayment profile in later years. These include adjustable rate mortgages (ARMs), loans in which the interest rate is periodically adjusted based on an index.

In recent years, the US has seen a significant change in the structure of borrowing products in the mortgage market. In particular, in the period from 2004 to 2006, affordability mortgages grew faster than more traditional fixed rate mortgages. Affordability mortgages included introductory interest-only, stated-income (low documentation), ARMs with alternative payment options (known as option ARMs), negatively amortising and layered risk loans, the latter including secondary loans. The growth of affordability mortgages occurred concurrently with gradually rising loan-to-value ratios.

Stated-income loans have a lesser income documentation requirement during the underwriting process and, accordingly, carry a higher risk.

Introductory interest-only loans allow customers to pay only accruing interest for a period of time, and provide customers with repayment flexibility. Secondary loans which are, for example, drawn down to finance the costs of relocation and property acquisition, are also increasingly common.

As a consequence of rising delinquency among sub-prime affordability mortgages which emerged in the second half of 2006, the market for resale of such mortgages contracted markedly in the first half of 2007. In March 2007, HSBC Finance made the decision to stop purchasing new mortgages from correspondents and this, together with portfolio sales, had the effect of reducing mortgage services loan balances from US\$49.5 billion at 31 December 2006 to US\$41.4 billion at 30 June 2007. HSBC does not offer, and does not expect to offer, option ARMs or other negative amortisation products.

As with all lending, HSBC underwrites mortgages in accordance with criteria that take into account the particular terms of the loan, and prices affordability mortgages in a manner designed to compensate for their higher risk.

The following table shows the level of mortgage products in the various portfolios of HSBC Finance and the rest of the HSBC Group.

|   | At 30 June 2007           |                |                | At 30 June 2006           |                |                | At 31 December 2006        |                |                |
|---|---------------------------|----------------|----------------|---------------------------|----------------|----------------|----------------------------|----------------|----------------|
|   | HSBC<br>Finance1<br>US\$m | Other<br>US\$m | Total<br>US\$m | HSBC<br>Finance1<br>US\$m | Other<br>US\$m | Total<br>US\$m | HSBC<br>Finance 1<br>US\$m | Other<br>US\$m | Total<br>US\$m |
| Total mortgage lending <sup>2</sup>           | <b>94,306</b>             | <b>194,221</b> | <b>288,527</b> | 95,895                    | 182,290        | 278,185        | 99,150                     | 189,348        | 288,498        |
| Interest only (including endowment) mortgages |                           | <b>34,735</b>  | <b>34,735</b>  |                           | 30,773         | 30,773         |                            | 33,190         | 33,190         |
| Affordability mortgages, including ARMs       | <b>21,876</b>             | <b>62,077</b>  | <b>83,953</b>  | 30,943                    | 58,766         | 89,709         | 30,169                     | 60,106         | 90,275         |
| Other   |                           | <b>415</b>     | <b>415</b>     |                           | 406            | 406            |                            | 295            | 295            |

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|  |               |               |                |        |        |         |        |        |         |
|--|---------------|---------------|----------------|--------|--------|---------|--------|--------|---------|
| Total interest only and affordability lending                    | <b>21,876</b> | <b>97,227</b> | <b>119,103</b> | 30,943 | 89,945 | 120,888 | 30,169 | 93,591 | 123,760 |
| As a percentage of total mortgage lending                        | <b>23.2%</b>  | <b>50.1%</b>  | <b>41.3%</b>   | 32.3%  | 49.3%  | 43.5%   | 30.4%  | 49.4%  | 42.9%   |
| Second lien mortgages  | <b>17,911</b> | <b>4,843</b>  | <b>22,754</b>  | 19,626 | 4,873  | 24,499  | 19,420 | 4,938  | 24,358  |
| As a percentage of total mortgage lending                        | <b>19.0%</b>  | <b>2.5%</b>   | <b>7.9%</b>    | 20.5%  | 2.7%   | 8.8%    | 19.6%  | 2.6%   | 8.4%    |
| Negative equity <sup>2</sup>                                     | <b>12,535</b> | <b>1,418</b>  | <b>13,953</b>  | 13,622 | 2,239  | 15,861  | 12,347 | 2,450  | 14,797  |
| Other loan to value ratios greater than 90 per cent <sup>3</sup> | <b>40,471</b> | <b>16,789</b> | <b>57,260</b>  | 41,167 | 17,160 | 58,327  | 45,712 | 19,608 | 65,320  |
|  | <b>53,006</b> | <b>18,207</b> | <b>71,213</b>  | 54,789 | 19,399 | 74,188  | 58,059 | 22,058 | 80,117  |
| As a percentage of total mortgage lending                        | <b>56.2%</b>  | <b>9.4%</b>   | <b>24.7%</b>   | 57.1%  | 10.6%  | 26.7%   | 58.6%  | 11.6%  | 27.8%   |

1 *HSBC Finance is shown on a management basis and includes lending in Canada and the UK and loans transferred to HSBC USA Inc. which are managed by HSBC Finance.*

2 *Total mortgage lending includes residential mortgages and second lien mortgage lending included within Other personal lending .*

3 *Loan to value ratios are generally based on values at origination date.*

4 *Amounts restated to show HSBC Finance management basis, consistent with current year.*



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## Mortgage lending in the US

Mortgage lending in the US includes loans and advances to customers with a first lien interest over a property. These balances are secured and are reported within residential mortgages. Loans with only a second lien are reported in other personal lending. The commentary that follows discusses both residential mortgages and second lien loans included within other personal lending.

HSBC continues to monitor a range of trends affecting the US mortgage lending industry. Housing markets in a large part of the US have been affected by a general slowing in the rate of appreciation in property values, or an actual decline in some markets, while the period of time properties remain unsold has increased. In addition, the ability of some borrowers to service their ARMs has been compromised as interest rates have risen, increasing the amounts payable on their loans as prices reset higher under their contracts. The effects of interest rate adjustments on first mortgages are also estimated to have had a direct impact on borrowers' ability to repay second lien mortgages taken out on the same properties. Similarly, as introductory interest-only mortgages move beyond the interest-only payment period, the ability of borrowers to make the increased payments is expected to be strained. The rating agencies have recently announced their intention to downgrade a number of debt issues secured by sub-prime mortgages. This could reduce market liquidity for sub-prime mortgages, cause further tightening of underwriting criteria and lead to higher interest rates on mortgages, which would result in a reduction of refinancing opportunities available to ARM customers and a consequent increase in expected defaults. Studies published in the US, and HSBC's own experience, indicate that mortgages originated throughout the industry in 2005 and 2006 are performing worse than loans originated in prior periods.

The effects of these recent trends have been concentrated in the mortgage services business which, until March 2007, purchased first and second lien mortgages from a network of third party lenders. As detailed in the table below, this business has approximately US\$41.4 billion of loans and advances outstanding from personal customers, 8.5 per cent of the Group's gross loans and advances to personal customers. At 31 December 2006, the business had US\$49.5 billion of loans and advances to personal customers which represented 10.4 per cent of the equivalent Group total. This decrease was mainly due to the decision to stop acquisitions from correspondents, to the repayment, refinancing and

write-off of balances owing and to HSBC's sale of certain mortgage loans.

In 2005 and continuing into the first six months of 2006, second lien mortgage loans in mortgage services increased significantly as a percentage of total loans acquired compared with previous periods. During the second quarter of 2006, HSBC began to experience deterioration in the credit performance of mortgages acquired in 2005. The deterioration continued in the second half of 2006 and began to affect loans acquired in that year. In the fourth quarter, the deterioration in the first lien ARM portfolio and loans in the second lien portfolios worsened considerably. HSBC continued to experience higher delinquency levels in the first half of 2007, although the rate of increase in delinquency in 2007 slowed compared with the previous year. A significant number of HSBC Finance's second lien customers have underlying first lien ARMs that face repricing in the near term which, based on experience, is likely to adversely affect the probability of default on the related second lien mortgages. This arises from the increase in payments required at the end of the introductory interest only period or following the rate reset date. It is estimated that, as interest rates have risen, credit availability has tightened and there has been either a decline in property values or a slowdown in the rate of their appreciation, the probability of default on ARM first mortgages subject to repricing, and on any second lien mortgage loans that are subordinate to first lien ARMs, is greater than has been experienced in the past. As a result, loan impairment charges related to the mortgage services portfolio are expected to remain high.

A number of steps have been taken to mitigate risk in the affected parts of the portfolio. These include enhanced segmentation and analytics to identify the higher risk portions of the portfolio, and increased collections capacity. HSBC Finance is restructuring or modifying loans in accordance with defined policies if it believes that customers will continue to repay their loan. Also, customers who have ARM loans nearing the first reset, and who are expected to be the most affected by a rate adjustment, are being contacted in order to assess their ability to make the higher payments and, as appropriate, refinance or modify their loans. As part of this proactive ARM management strategy, HSBC Finance has contacted over 19,000 customers to date, either by telephone or in writing, and has modified the loans of 5,000 of them. The second half of 2007 will see a further increase in this activity.

HSBC Finance has implemented repricing initiatives in selected segments of the originated

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loans and tightened underwriting criteria, especially for second lien, stated-income and other higher risk segments. These actions, combined with the decision to stop purchasing new mortgages from correspondents, the sale during the first half of 2007 of US\$2.7 billion of non-delinquent loans, and normal repayments have resulted in a net reduction in loans and advances in mortgage services since June 2006. The loan sales did not include any loans that were 30 days or more delinquent.

While it is expected that this portfolio will reduce more quickly than other loan books, portions of the portfolio will remain under pressure as loans originated in 2005 and 2006 continue to season and a higher proportion of loans than usual progress to various stages of delinquency and write-off.

The Decision One wholesale operation, which acquires loans through brokers for resale in the

secondary market, and the branch-based consumer lending business retail channel have continued underwriting loans, albeit with tightened credit underwriting criteria.

The Federal Financial Regulatory Agencies recently issued a final statement on sub-prime mortgage lending. The guidance reiterates many of the existing principles related to risk management practices and consumer protection laws involving ARM products and the underwriting process on stated income and interest-only loans. Although a significant portion of HSBC Finance's business is already substantially in compliance with the new guidance, a full assessment of the effect is currently under way and HSBC anticipates being fully compliant with the new guidelines by the end of the year.

**Mortgage loan balances in HSBC Finance**<sup>1</sup>

|                            | At 30 June 2007            |                           |  | At 30 June 2006            |                           |  | At 31 December 2006 <sup>2</sup> |                           |  |
|----------------------------|----------------------------|---------------------------|--|----------------------------|---------------------------|--|----------------------------------|---------------------------|--|
|                            | Mortgage services<br>US\$m | Consumer lending<br>US\$m | Other mortgage lending <sup>3</sup><br>US\$m | Mortgage services<br>US\$m | Consumer lending<br>US\$m | Other mortgage lending <sup>3</sup><br>US\$m | Mortgage services<br>US\$m       | Consumer lending<br>US\$m | Other mortgage lending <sup>3</sup><br>US\$m |
| Fixed rate                 | 22,391                     | 45,369                    | 2,471  | 24,908                     | 38,838                    | 2,151  | 22,358                           | 42,378                    | 2,207  |
| Adjustable rate            | 18,991                     | 3,406                     | 1,676  | 26,538                     | 2,028                     | 1,432  | 27,114                           | 3,528                     | 1,562  |
| <b>Total</b>               | <b>41,382</b>              | <b>48,775</b>             | <b>4,147</b>                                 | <b>51,446</b>              | <b>40,866</b>             | <b>3,583</b>                                 | <b>49,472</b>                    | <b>45,906</b>             | <b>3,769</b>                                 |
| First lien                 | 33,137                     | 42,234                    | 1,022  | 40,126                     | 35,294                    | 849  | 39,404                           | 39,406                    | 917  |
| Second lien                | 8,245                      | 6,541                     | 3,125  | 11,320                     | 5,572                     | 2,734  | 10,068                           | 6,500                     | 2,852  |
| <b>Total</b>               | <b>41,382</b>              | <b>48,775</b>             | <b>4,147</b>                                 | <b>51,446</b>              | <b>40,866</b>             | <b>3,583</b>                                 | <b>49,472</b>                    | <b>45,906</b>             | <b>3,769</b>                                 |
| Adjustable rate            | 14,402                     | 3,406                     | 1,676  | 20,398                     | 2,028                     | 1,432  | 21,344                           | 3,528                     | 1,562  |
| Introductory interest only | 4,589                      |                           |  | 6,140                      |                           |  | 5,770                            |                           |  |

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|                       |               |              |              |        |       |       |        |       |       |
|-----------------------|---------------|--------------|--------------|--------|-------|-------|--------|-------|-------|
| Total adjustable rate | <b>18,991</b> | <b>3,406</b> | <b>1,676</b> | 26,538 | 2,028 | 1,432 | 27,114 | 3,528 | 1,562 |
|-----------------------|---------------|--------------|--------------|--------|-------|-------|--------|-------|-------|

- 1 *Management basis.*
- 2 *Amounts restated to show HSBC Finance management basis, consistent with current year.*
- 3 *Includes balances in the UK and Canada.*

The above table summarises mortgage balance information for the mortgage services and consumer lending businesses within HSBC Finance. Mortgages include first lien residential mortgages and second lien mortgage lending, the latter being reported within other personal lending in the market sector analysis on page 96.

At 30 June 2007, the outstanding balance of introductory interest-only loans in the mortgage services business was US\$4.6 billion, or 0.9 per cent of the Group's gross loans and advances to personal customers, a fall of 20 per cent compared with the US\$5.8 billion, or 1.2 per cent of loans at the end of 2006.

The outstanding balance of ARMs in the mortgage services business at 30 June 2007 declined by 30 per cent compared with the end of 2006 to US\$19.0 billion, 3.9 per cent of the Group's gross loans and advances to personal customers.

At the end of 2006, US\$10.7 billion of ARMs were due to reach their first interest rate reset in 2007, of which US\$9.9 billion related to mortgage services. US\$7 billion of the mortgage services resets were due in the second half of 2007. During the first half of 2007, US\$1.7 billion of ARMs reset and are still held by HSBC. Repayments, loan sales, write-offs and modifications have reduced the amount of interest rate resets in the second half of 2007, and the current position is that US\$5.8 billion

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of ARMs will reach their first reset in that period, of which US\$5.3 billion are in mortgage services.

In 2008, a further US\$4.1 billion of ARM loans reach their interest rate reset date for the first time in HSBC Finance, of which US\$3 billion is in mortgage services.

The balance of stated-income mortgages, all of which are in mortgage services, was approximately US\$9.4 billion at 30 June 2007, or 1.9 per cent of the Group's gross loans and advances to personal customers. At the end of 2006, the outstanding balance was US\$11.8 billion, or 2.5 per cent of loans.

**Impairment allowances and charges in mortgage services**

|  | Half-year to             |                          |                                 |
|--|--------------------------|--------------------------|---------------------------------|
|  | 30 June<br>2007<br>US\$m | 30 June<br>2006<br>US\$m | 31<br>December<br>2006<br>US\$m |
| Impairment allowances at the beginning of the period | 2,043                    | 428                      | 548                             |
| Loan impairment charges                              | 760                      | 338                      | 1,833                           |
| Net amounts written off                              | (680)                    | (209)                    | (334)                           |
| Other movements                                      | (27)                     | (9)                      | (4)                             |
| Impairment allowances at the end of the period       | 2,096                    | 548                      | 2,043                           |

**Credit quality**

The following tables set out the distribution of loans and advances by measures of credit quality, an ageing analysis of loans and advances that were past due but not impaired, and a geographical breakdown of impaired loans and related impairment allowances.

These reflect broadly stable credit quality across the majority of the Group's businesses, commensurate with the growth in lending volumes.

Within this, the deterioration in quality in US mortgage portfolios and, to a lesser extent, in UK personal unsecured portfolios, is fully commented on elsewhere in this report. The credit quality of loans and advances to banks remained high and stable.

There was no material change in the age profile shown in the ageing analysis of past due loans and advances. The coverage ratio of impairment allowances to impaired loans remained at a similar high level to that reached at 31 December 2006.

Distribution of loans and advances by credit quality

| At 30 June 2007       |                       | At 30 June 2006       |                       | At 31 December 2006   |                       |
|-----------------------|-----------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| Loans and advances to | Loans and advances to | Loans and advances to | Loans and advances to | Loans and advances to | Loans and advances to |

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|                               | customers<br>US\$m | banks<br>US\$m | customers <sup>1</sup><br>US\$m | banks<br>US\$m | customers <sup>1</sup><br>US\$m | banks<br>US\$m |
|-------------------------------|--------------------|----------------|---------------------------------|----------------|---------------------------------|----------------|
| Loans and advances:           |                    |                |                                 |                |                                 |                |
| neither past due nor impaired | 885,815            | 214,277        | 779,385                         | 162,395        | 827,495                         | 185,125        |
| past due but not impaired     | 42,054             | 363            | 33,909                          | 78             | 40,431                          | 72             |
| impaired                      | 14,555             | 12             | 12,296                          | 17             | 13,785                          | 15             |
|                               | <u>942,424</u>     | <u>214,652</u> | <u>825,590</u>                  | <u>162,490</u> | <u>881,711</u>                  | <u>185,212</u> |

1 The amounts reported for periods in 2006 as *past due but not impaired* have been amended to include certain loans previously classified as *neither past due nor impaired*. The reclassification reflects the fact that, while these loans are in early-stage arrears, a proportion arise from events unrelated to poor credit quality, and historical experience suggests that only a small percentage of such loans progresses through stages of delinquency to default. This reclassification has no effect on total impaired loans or impairment allowances.

Examples of exposures designated *past due but not considered impaired* include: loans fully secured by cash collateral; residential mortgages in arrears 90 days or more, but where the value of collateral is sufficient to repay both the principal debt and all potential interest for at least one year; and short-term trade facilities past due 90 days or more for technical reasons such as delays in documentation, but where there is no concern over the creditworthiness of the counterparty.

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Loans and advances which were past due but not impaired

Loans and advances which were past due at 30 June 2007, 30 June 2006 and 31 December 2006 but not impaired were as follows:

|                        | At 30 June 2007                          |                                      | At 30 June 2006                                       |                                      | At 31 December 2006                                   |                                      |
|------------------------|--|--------------------------------------|---|--------------------------------------|---|--------------------------------------|
|                        | Loans and advances to customers<br>US\$m | Loans and advances to banks<br>US\$m | Loans and advances to customers <sup>1</sup><br>US\$m | Loans and advances to banks<br>US\$m | Loans and advances to customers <sup>1</sup><br>US\$m | Loans and advances to banks<br>US\$m |
| Past due up to 29 days | 29,243                                   | 363                                  | 23,600  | 78                                   | 28,359  | 72                                   |
| Past due 30 - 59 days  | 7,766                                    |                                      | 6,381   |                                      | 7,353   |                                      |
| Past due 60 - 89 days  | 3,014                                    |                                      | 2,324   |                                      | 2,796   |                                      |
|                        | <b>40,023</b>                            | <b>363</b>                           | 32,305  | 78                                   | 38,508  | 72                                   |
| Past due 90 - 179 days | 1,733                                    |                                      | 1,516   |                                      | 1,764   |                                      |
| Past due over 180 days | 298                                      |                                      | 88  |                                      | 159   |                                      |
|                        | <b>42,054</b>                            | <b>363</b>                           | 33,909  | 78                                   | 40,431  | 72                                   |

Impaired customer loans and impairment allowances by geographical region

|                      | At 30 June 2007         |                                | At 30 June 2006<br>(restated <sup>1</sup> ) |                                | At 31 December 2006     |                                |
|----------------------|-------------------------|--------------------------------|---|--------------------------------|-------------------------|--------------------------------|
|                      | Impaired loans<br>US\$m | Impairment allowances<br>US\$m | Impaired loans<br>US\$m                     | Impairment allowances<br>US\$m | Impaired loans<br>US\$m | Impairment allowances<br>US\$m |
| Europe               | 5,849                   | 3,643                          | 5,767                                       | 3,513                          | 5,847                   | 3,676                          |
| Hong Kong            | 467                     | 335                            | 504   | 391                            | 454                     | 365                            |
| Rest of Asia-Pacific | 1,209                   | 940                            | 1,041                                       | 910                            | 1,184                   | 901                            |
| North America        | 5,226                   | 7,714                          | 3,638                                       | 5,249                          | 4,822                   | 7,247                          |
| Latin America        | 1,804                   | 1,691                          | 1,346                                       | 1,318                          | 1,478                   | 1,389                          |
|                      | <b>14,555</b>           | <b>14,323</b>                  | 12,296                                      | 11,381                         | 13,785                  | 13,578                         |

<sup>1</sup> In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

Total impaired loans to customers were US\$14,555 million at 30 June 2007, an increase of 6 per cent since the end of 2006. At constant currency, the growth was 4 per cent, and impaired loans were 2 per cent of gross customer loans and advances, broadly in line with 31 December

2006.

The commentary that follows compares balances at 30 June 2007 with those on 31 December 2006, at constant exchange rates.

In **Europe**, impaired loans decreased by 2 per cent to US\$5,849 million, primarily due to the write-off of personal loans in the UK that were fully provided for, although this was partly offset by higher impaired loans in M&S branded credit cards, due to growth in balances and the seasoning of the portfolio. Tighter underwriting in the UK personal lending portfolio and higher write-offs driven by the upward trend in bankruptcies and IVAs, further contributed to the decrease in impaired loans. Impaired loans in France stayed broadly in line with 31 December 2006, and an 11 per cent increase in Turkey reflected growth in customer advances. The credit environment in these countries remained stable.

In **Hong Kong**, impaired loans were slightly higher at US\$467 million, driven by significant lending growth. The strong economy helped to underpin a stable credit environment.

In **Rest of Asia-Pacific**, impaired loans increased modestly to US\$1,209 million, mainly driven by higher delinquencies in Thailand resulting from a single corporate customer. In India, impaired loans increased in line with significant growth in personal loan balances. These increases were largely offset by lower impaired loan balances in Malaysia resulting from the reclassification of a portfolio of non-performing mortgages as assets held for sale pending finalisation of its disposal, and reduced card impairment in Taiwan due to the improving credit environment there.

In **North America**, there was an 8 per cent rise in impaired loans to US\$5,226 million at 30 June 2007. In the mortgage services correspondent business, the credit deterioration experienced in the second lien and certain first lien mortgages originated in 2005 and 2006 continued to put upward pressure on reported delinquency rates. This will continue to increase as the portfolio is reduced. The

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implementation of various initiatives led to a considerable decline in outstanding loans. These included new pricing structures, significantly tighter underwriting criteria, and reductions in the purchases of second lien and selected higher risk products. This culminated in the decision in March 2007 to stop purchasing mortgages from correspondents.

The consumer lending business in the US experienced higher loan impairment, mainly as a result of balance sheet growth and portfolio seasoning. The discontinuation of certain unprofitable segments of the unsecured portfolio and tighter underwriting criteria in direct mail originations, were offset by a deterioration in real estate and personal home loans. Credit card impairment rose, reflecting the recent growth in advances and the return of bankruptcies to normal levels following the legislative changes in the fourth quarter of 2005 and the resulting lower levels of bankruptcies throughout 2006.

In **Latin America**, impaired loans increased by 14 per cent to US\$1,804 million. In Mexico, in line with the strategy to grow HSBC's business in segments where the Group has had a modest market presence, continuing growth of the credit card portfolio and small business lending led to a corresponding 28 per cent growth in impaired loans.

### Renegotiated loans

Restructuring activity is designed to manage customer relationships, maximise collection opportunities and, if possible, avoid foreclosure or repossession. Such activities include extended payment arrangements, approved external debt management plans, deferring foreclosure, modification, loan rewrites and/or deferral of payments pending a change in circumstances. Following restructuring, an overdue consumer account is normally reset from delinquent to current status. Restructuring policies and practices are based on indicators or criteria which, in the judgement of local management, indicate that repayment will probably continue. These policies are required to be kept under continual review and their application varies according to the nature of the market, the product, and the availability of empirically based data. When empirical evidence indicates an increased propensity to default on restructured accounts, the use of roll rate methodology ensures this factor is taken into account when calculating impairment allowances.

Restructuring is most commonly applied to consumer finance portfolios. HSBC Finance had US\$20.6 billion of such loans at 30 June 2007, an increase of approximately 20 per cent since 31 December 2006, equating to some 85 per cent of the total Group renegotiated loans. The increase was substantially driven by higher levels of mortgage renegotiations in mortgage services.

### Impairment allowances and charges

Movement in allowance accounts for total loans and advances

|  | <b>Individually<br/>assessed<br/>US\$m</b> | <b>Collectively<br/>assessed<br/>US\$m</b> | <b>Total<br/>US\$m</b> |
|--|--|--|------------------------|
| At 1 January 2007  | 2,572                                      | 11,013                                     | 13,585                 |
| Amounts written off  | (390)                                      | (5,673)                                    | (6,063)                |
| Recoveries of loans and advances written off in previous years | 57   | 287  | 344                    |
| Charge to income statement                                     | 385  | 5,943                                      | 6,328                  |
| Exchange and other movements                                   | (3)  | 139  | 136                    |
|  | <hr/>                                      | <hr/>                                      | <hr/>                  |
| At 30 June 2007  | <b>2,621</b>                               | <b>11,709</b>                              | <b>14,330</b>          |
|  | <hr/>                                      | <hr/>                                      | <hr/>                  |
| At 1 January 2006  | 2,679                                      | 8,687                                      | 11,366                 |
| Amounts written off  | (551)                                      | (3,887)                                    | (4,438)                |
| Recoveries of loans and advances written off in previous years | 75   | 268  | 343                    |
| Charge to income statement                                     | 178  | 3,718                                      | 3,896                  |
| Exchange and other movements                                   | (12)                                       | 234  | 222                    |
|  | <hr/>                                      | <hr/>                                      | <hr/>                  |
| At 30 June 2006  | 2,369                                      | 9,020                                      | 11,389                 |



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|  |       |         |         |
|--|-------|---------|---------|
| At 1 July 2006   | 2,369 | 9,020   | 11,389  |
| Amounts written off  | (472) | (4,563) | (5,035) |
| Recoveries of loans and advances written off in previous years | 53    | 383     | 436     |
| Charge to income statement                                     | 280   | 6,371   | 6,651   |
| Exchange and other movements                                   | 342   | (198)   | 144     |
| At 31 December 2006  | 2,572 | 11,013  | 13,585  |

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HSBC HOLDINGS PLC

**The Management of Risk** (continued)

Net loan impairment charge to the income statement by geographical region

|   | <b>Half-year to 30 June 2007</b> |                  |                             |                      |                      |              |
|---|----------------------------------|------------------|-----------------------------|----------------------|----------------------|--------------|
|   | <b>Europe</b>                    | <b>Hong Kong</b> | <b>Rest of Asia-Pacific</b> | <b>North America</b> | <b>Latin America</b> | <b>Total</b> |
|   | <b>US\$m</b>                     | <b>US\$m</b>     | <b>US\$m</b>                | <b>US\$m</b>         | <b>US\$m</b>         | <b>US\$m</b> |
| <b>Individually assessed impairment allowances</b>  |                                  |                  |                             |                      |                      |              |
| New allowances  | 406                              | 40               | 130                         | 122                  | 77                   | 775          |
| Releases of allowances no longer required   | (228)                            | (10)             | (53)                        | (25)                 | (17)                 | (333)        |
| Recoveries of amounts previously written off  | (17)                             | (6)              | (15)                        | (15)                 | (4)                  | (57)         |
|   | <b>161</b>                       | <b>24</b>        | <b>62</b>                   | <b>82</b>            | <b>56</b>            | <b>385</b>   |
| <b>Collectively assessed impairment allowances</b>  |                                  |                  |                             |                      |                      |              |
| New allowances net of allowance releases  | 1,310                            | 72               | 291                         | 3,763                | 794                  | 6,230        |
| Recoveries of amounts previously written off  | (131)                            | (14)             | (45)                        | (17)                 | (80)                 | (287)        |
|   | <b>1,179</b>                     | <b>58</b>        | <b>246</b>                  | <b>3,746</b>         | <b>714</b>           | <b>5,943</b> |
| Total charge for impairment losses on loans and advances                                      | <b>1,340</b>                     | <b>82</b>        | <b>308</b>                  | <b>3,828</b>         | <b>770</b>           | <b>6,328</b> |
| to banks  |                                  |                  |                             |                      |                      |              |
| to customers  | <b>1,340</b>                     | <b>82</b>        | <b>308</b>                  | <b>3,828</b>         | <b>770</b>           | <b>6,328</b> |
|   | <i>%</i>                         | <i>%</i>         | <i>%</i>                    | <i>%</i>             | <i>%</i>             | <i>%</i>     |
| Charge for impairment losses as a percentage of closing gross loans and advances (annualised) | <b>0.53</b>                      | <b>0.10</b>      | <b>0.50</b>                 | <b>2.51</b>          | <b>2.79</b>          | <b>1.10</b>  |

Half-year to 30 June 2006 (restated<sup>1</sup>)

|  | <b>Europe</b> | <b>Hong Kong</b> | <b>Rest of Asia-Pacific</b> | <b>North America</b> | <b>Latin America</b> | <b>Total</b> |
|--|---------------|------------------|-----------------------------|----------------------|----------------------|--------------|
|  | <b>US\$m</b>  | <b>US\$m</b>     | <b>US\$m</b>                | <b>US\$m</b>         | <b>US\$m</b>         | <b>US\$m</b> |
| <b>Individually assessed impairment allowances</b> |               |                  |                             |                      |                      |              |
| New allowances                                     | 351           | 50               | 87                          | 110                  | 61                   | 659          |
| Releases of allowances no longer required          | (251)         | (30)             | (79)                        | (29)                 | (17)                 | (406)        |
| Recoveries of amounts previously written off       | (19)          | (8)              | (13)                        | (23)                 | (12)                 | (75)         |
|  | <b>81</b>     | <b>12</b>        | <b>(5)</b>                  | <b>58</b>            | <b>32</b>            | <b>178</b>   |

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|   |       |      |      |       |      |       |
|---|-------|------|------|-------|------|-------|
| Collectively assessed impairment allowances   |       |      |      |       |      |       |
| New allowances net of allowance releases  | 981   | 67   | 308  | 2,159 | 471  | 3,986 |
| Recoveries of amounts previously written off  | (122) | (13) | (31) | (43)  | (59) | (268) |
|   | 859   | 54   | 277  | 2,116 | 412  | 3,718 |
| Total charge for impairment losses on loans and advances                                      | 940   | 66   | 272  | 2,174 | 444  | 3,896 |
| to banks  |       |      |      |       |      |       |
| to customers  | 940   | 66   | 272  | 2,174 | 444  | 3,896 |
|   |       |      |      |       |      |       |
|   | %     | %    | %    | %     | %    | %     |
| Charge for impairment losses as a percentage of closing gross loans and advances (annualised) | 0.44  | 0.10 | 0.54 | 1.51  | 2.50 | 0.79  |

1 In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

[Back to Contents](#)Net loan impairment charge to the income statement by geographical region *(continued)*

|   | Half-year to 31 December 2006 |                       |                                      |                           |                           |                |
|---|-------------------------------|-----------------------|--------------------------------------|---------------------------|---------------------------|----------------|
|   | Europe<br>US\$m               | Hong<br>Kong<br>US\$m | Rest of<br>Asia-<br>Pacific<br>US\$m | North<br>America<br>US\$m | Latin<br>America<br>US\$m | Total<br>US\$m |
| <b>Individually assessed impairment allowances</b>  |                               |                       |                                      |                           |                           |                |
| New allowances  | 364                           | 43                    | 51                                   | 119                       | 61                        | 638            |
| Releases of allowances no longer required   | (188)                         | (15)                  | (51)                                 | (32)                      | (19)                      | (305)          |
| Recoveries of amounts previously written off  | (14)                          | (6)                   | (15)                                 | (16)                      | (2)                       | (53)           |
|   | <u>162</u>                    | <u>22</u>             | <u>(15)</u>                          | <u>71</u>                 | <u>40</u>                 | <u>280</u>     |
| <b>Collectively assessed impairment allowances</b>  |                               |                       |                                      |                           |                           |                |
| New allowances net of allowance releases  | 1,304                         | 83                    | 291                                  | 4,556                     | 520                       | 6,754          |
| Recoveries of amounts previously written off  | (266)                         | (14)                  | (36)                                 | (3)                       | (64)                      | (383)          |
|   | <u>1,038</u>                  | <u>69</u>             | <u>255</u>                           | <u>4,553</u>              | <u>456</u>                | <u>6,371</u>   |
| <b>Total charge for impairment losses on loans and advances</b>                               |                               |                       |                                      |                           |                           |                |
| to banks  | 1,200                         | 91                    | 240                                  | 4,624                     | 496                       | 6,651          |
| to customers  | 1,200                         | 91                    | 241                                  | 4,624                     | 498                       | 6,654          |
|   | <u>1,200</u>                  | <u>91</u>             | <u>241</u>                           | <u>4,624</u>              | <u>498</u>                | <u>6,654</u>   |
|   | %                             | %                     | %                                    | %                         | %                         | %              |
| Charge for impairment losses as a percentage of closing gross loans and advances (annualised) | 0.51                          | 0.14                  | 0.45                                 | 3.07                      | 2.00                      | 1.25           |

Loan impairment charges increased to US\$6,328 million, a rise of 62 per cent compared with the first half of 2006. The commentary that follows is on a constant currency basis:

New allowances for loan impairment charges rose by 45 per cent, compared with the first half of 2006, to US\$7,005 million. Releases and recoveries of allowances decreased by 17 per cent to US\$677 million.

In **Europe**, new loan impairment charges were US\$1,716 million, a rise of 18 per cent compared with the first half of 2006. Excluding the effect of refinements in the methodology used to calculate roll rate percentages in the UK consumer finance business, new loan impairment charges increased due to growth in credit card lending and upward market trends in personal bankruptcies and IVAs. As a result, HSBC curtailed lending to some higher-risk borrowers. Impairment charges also increased modestly in France and Turkey, but overall credit quality remained stable.

Releases and recoveries in Europe were US\$376 million, a fall of 16 per cent, mainly due to a sale of a portfolio of loans in France.

In **Hong Kong**, new loan impairment charges were broadly in line with the first half of 2006 at US\$112 million.

Releases and recoveries in Hong Kong decreased to US\$30 million, primarily in the corporate sector.

In **Rest of Asia-Pacific**, new loan impairment charges increased slightly to US\$421 million. In India and Malaysia, higher loan impairment charges arose from significant increases in consumer lending and, in Malaysia and Thailand, new loan impairment charges related to a single corporate customer in each country. The improved credit environment in Taiwan and Indonesia resulted in lower loan impairment charges on credit cards.

Releases and recoveries decreased by 12 per cent to US\$113 million, mainly due to lower releases in the Middle East.

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In **North America**, new loan impairment charges increased by 71 per cent to US\$3,885 million as a result of higher customer loan balances and a rise in delinquency rates, the latter attributable to normal portfolio seasoning and the progression of mortgage services portfolios purchased in 2005 and 2006 into various stages of delinquency and write-off. The increase in new loan impairment charges was also driven by a rise in the proportion of unsecured loans such as credit cards and personal lending, higher levels of personal bankruptcy filings compared with the exceptionally low levels experienced in the first half of 2006 (as a result of the new US bankruptcy law which took

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**The Management of Risk** (continued)

effect in October 2005) and the weakening, in line with industry trends, of some consumer lending mortgages underwritten since late 2005. In mortgage services, portfolio seasoning and deterioration in second lien and portions of first lien mortgages acquired from correspondents in 2005 and the first half of 2006 resulted in higher charges. In March 2007, HSBC made the decision to stop purchasing new mortgages from correspondents. Elevated delinquency rates continued in 2007, although the rate of increase in delinquency slowed compared with the full year of 2006. Consumer lending and card services also experienced higher charges due to balance growth and portfolio seasoning. Strong asset

growth and higher delinquency rates in the motor vehicle finance business led to higher loan impairment charges in Canada.

Releases and recoveries in North America decreased to US\$57 million, mainly due to lower recoveries in the US consumer finance business.

In **Latin America**, new loan impairment charges rose by 54 per cent to US\$871 million. In Mexico, planned growth in the credit and small business segments led to increased loan impairment charges.

Releases and recoveries in Latin America were broadly in line with the first half of 2006.

## Loan delinquency in the US

The following table summarises two-months-and-over contractual delinquency (as a percentage of loans and advances) within Personal Financial Services in the US:

|                              | Quarter ended           |                          |  |   |                                      |                                       |                             |   |
|------------------------------|-------------------------|--------------------------|--|---|--------------------------------------|---------------------------------------|-----------------------------|---|
|                              | 30<br>June<br>2007<br>% | 31<br>March<br>2007<br>% | 31<br>December<br>2006 <sup>1</sup><br>% | 30<br>September<br>2006 <sup>1</sup><br>% | 30<br>June<br>2006 <sup>1</sup><br>% | 31<br>March<br>2006 <sup>1</sup><br>% | 31<br>December<br>2005<br>% | 30<br>September<br>2005 <sup>1</sup><br>% |
| Residential mortgages        | 2.92                    | 2.54                     | 2.54                                     | 2.21                                      | 1.92                                 | 1.82                                  | 2.04                        | 1.76                                      |
| Second lien mortgage lending | 5.06                    | 4.38                     | 4.00                                     | 2.72                                      | 1.86                                 | 1.77                                  | 1.60                        | 1.38                                      |
| Vehicle finance <sup>2</sup> | 2.91                    | 2.29                     | 3.16                                     | 3.21                                      | 2.82                                 | 2.27                                  | 3.28                        | 3.10                                      |
| Credit card <sup>3</sup>     | 4.32                    | 4.43                     | 4.48                                     | 4.46                                      | 4.09                                 | 4.28                                  | 3.46                        | 4.06                                      |
| Private label                | 2.72                    | 2.65                     | 2.83                                     | 2.88                                      | 2.84                                 | 2.60                                  | 2.41                        | 2.54                                      |
| Personal non-credit card     | 9.69                    | 9.33                     | 9.05                                     | 8.23                                      | 7.56                                 | 7.70                                  | 8.58                        | 8.28                                      |
| Total <sup>3</sup>           | 4.01                    | 3.65                     | 3.67                                     | 3.29                                      | 2.89                                 | 2.81                                  | 2.97                        | 2.81                                      |

Residential mortgages and second lien mortgage lending with two-months-and-over contractual delinquency (as a percentage of loans and advances) for the mortgage services and consumer lending portfolios comprised the following:

|  | Quarter ended |    |    |    |    |    |    |    |
|--|---------------|----|----|----|----|----|----|----|
|  | 30            | 31 | 31 | 30 | 30 | 31 | 31 | 30 |
|  |               |    |    |    |    |    |    |    |

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|                                  | <b>June<br/>2007</b> | <b>March<br/>2007</b> | December<br>2006 <sup>1</sup> | September<br>2006 <sup>1</sup> | June<br>2006 <sup>1</sup> | March<br>2006 <sup>1</sup> | December<br>2005 <sup>1</sup> | September<br>2005 <sup>1</sup> |
|----------------------------------|----------------------|-----------------------|-------------------------------|--------------------------------|---------------------------|----------------------------|-------------------------------|--------------------------------|
|                                  | %                    | %                     | %                             | %                              | %                         | %                          | %                             | %                              |
| Mortgage services <sup>4</sup> : |                      |                       |                               |                                |                           |                            |                               |                                |
| first lien                       | <b>5.76</b>          | <b>4.53</b>           | 4.39                          | 3.68                           | 3.04                      | 2.80                       | 3.15                          | 2.78                           |
| second lien                      | <b>8.01</b>          | <b>6.50</b>           | 5.67                          | 3.64                           | 2.32                      | 1.80                       | 1.88                          | 1.46                           |
| Total mortgage services          | <b>6.21</b>          | <b>4.92</b>           | 4.65                          | 3.67                           | 2.88                      | 2.59                       | 2.92                          | 2.57                           |
| Consumer lending:                |                      |                       |                               |                                |                           |                            |                               |                                |
| first lien                       | <b>2.15</b>          | <b>2.03</b>           | 2.08                          | 1.92                           | 1.87                      | 1.90                       | 2.31                          | 2.27                           |
| second lien                      | <b>3.60</b>          | <b>3.34</b>           | 3.08                          | 2.03                           | 1.76                      | 2.61                       | 2.07                          | 2.04                           |
| Total consumer lending           | <b>2.34</b>          | <b>2.21</b>           | 2.22                          | 1.93                           | 1.86                      | 2.00                       | 2.28                          | 2.24                           |

1 *Delinquency data excludes mortgages held for sale. Prior period amounts have been restated accordingly.*

2 *In December 2006, the vehicle finance business changed its write-off policy to provide that the principal balance of vehicle loans in excess of the estimated net realisable value will be written off 30 days (previously 90 days) after the financed vehicle has been repossessed if it remains unsold, unless it becomes 150 days contractually delinquent, at which time such excess will be written off. This resulted in a one-time acceleration of write-off which totalled US\$24 million in December 2006. In connection with this policy change, the vehicle finance business also changed its methodology for reporting two-months-and-over contractual delinquency to include loan balances associated with repossessed vehicles which have not yet been written down to net realisable value. This resulted in an increase of 42 basis points to the vehicle finance delinquency ratio and an increase of 3 basis points to the total consumer delinquency ratio. Comparative information has been restated accordingly.*

3 *In December 2005, the acquisition of Metris was completed which included loans and advances of US\$5.3 billion. This event had an effect on this ratio from the date of acquisition because of the higher mix of sub-prime within the Metris portfolio.*

4 *The cessation of correspondent channel originations and portfolio sales affected the delinquency rate significantly. As the mortgage services portfolio decreases, the delinquency rate will continue to rise.*

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Charge for impairment losses as a percentage of average gross loans and advances to customers

|  | Europe<br>% | Hong<br>Kong<br>% | Rest of<br>Asia-<br>Pacific<br>% | North<br>America <sup>1</sup><br>% | Latin<br>America <sup>1</sup><br>% | Total<br>% |
|--|-------------|-------------------|----------------------------------|------------------------------------|------------------------------------|------------|
| <b>Half-year to 30 June 2007</b>         |             |                   |                                  |                                    |                                    |            |
| New allowances net of allowance releases | 0.89        | 0.24              | 0.89                             | 2.74                               | 4.41                               | 1.61       |
| Recoveries                               | (0.08)      | (0.04)            | (0.14)                           | (0.02)                             | (0.42)                             | (0.08)     |
| Impairment charges                       | 0.81        | 0.20              | 0.75                             | 2.72                               | 3.99                               | 1.53       |
| Amount written off net of recoveries     | 0.83        | 0.24              | 0.60                             | 2.40                               | 3.07                               | 1.39       |
| <b>Half-year to 30 June 2006</b>         |             |                   |                                  |                                    |                                    |            |
| New allowances net of allowance releases | 0.70        | 0.19              | 0.87                             | 1.71                               | 4.13                               | 1.16       |
| Recoveries                               | (0.08)      | (0.04)            | (0.14)                           | (0.06)                             | (0.56)                             | (0.12)     |
| Impairment charges                       | 0.62        | 0.15              | 0.73                             | 1.65                               | 3.57                               | 1.04       |
| Amount written off net of recoveries     | 0.71        | 0.15              | 0.66                             | 1.71                               | 3.59                               | 1.09       |
| <b>Half-year to 31 December 2006</b>     |             |                   |                                  |                                    |                                    |            |
| New allowances net of allowance releases | 0.99        | 0.26              | 0.75                             | 3.37                               | 4.05                               | 1.85       |
| Recoveries                               | (0.20)      | (0.04)            | (0.14)                           | (0.02)                             | (0.50)                             | (0.12)     |
| Impairment charges                       | 0.79        | 0.22              | 0.61                             | 3.35                               | 3.55                               | 1.73       |
| Amount written off net of recoveries     | 0.81        | 0.26              | 0.60                             | 1.88                               | 3.39                               | 1.21       |

<sup>1</sup> In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

### Risk elements in the loan portfolio

The disclosure of credit risk elements under the following headings reflects US accounting practice and classifications:

- loans accounted for on a non-accrual basis;
- accruing loans contractually past due 90 days or more as to interest or principal; and
- troubled debt restructurings not included in the above.

#### Impaired loans

In accordance with IFRSs, interest income continues to be recognised on assets that have been written down as a result of an impairment loss. In the following tables, HSBC presents information on its impaired loans and advances which are designated in accordance with the policy described above.

Impaired loans under IFRSs are consistent with the non-accrual basis classification used in US GAAP and in prior years.

#### Troubled debt restructurings



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US GAAP requires separate disclosure of any loans whose terms have been modified to grant concessions other than are warranted by market conditions because of problems with the borrower. These are classified as troubled debt restructurings and are distinct from the normal restructuring

activities in personal loan portfolios described in Renegotiated loans on page 107. Disclosure of a loan as a troubled debt restructuring may be discontinued after the first year if the debt performs in accordance with the new terms and they are in line with market conditions at the time of restructure.

The significant rise in troubled debt restructuring was mainly due to North America, driven by portfolio growth and recent action to contact customers ahead of ARM resets to modify or restructure loans.

### Unimpaired loans contractually past due 90 days or more

In common with other card issuers, including other parts of HSBC, HSBC Finance continues to accrue interest on credit cards over 90 days past due until written off. Appropriate allowances are raised against the proportion judged to be irrecoverable.

### Potential problem loans

Credit risk elements also cover potential problem loans. These are loans where information about borrowers possible credit problems causes management serious doubts about the borrowers ability to comply with the loan repayment terms. The table of risk elements set out below identifies, in addition to impaired loans, HSBC s significant potential problem loans.

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HSBC HOLDINGS PLC

**The Management of Risk** (continued)

Analysis of risk elements in the loan portfolio by geographical region

|  | At<br>30 June<br>2007<br>US\$m | At<br>30 June<br>2006<br>US\$m | At<br>31 December<br>2006<br>US\$m |
|--|--------------------------------|--------------------------------|------------------------------------|
| <b>Impaired loans</b>  |                                |                                |                                    |
| Europe   | 5,861                          | 5,778                          | 5,858                              |
| Hong Kong  | 467                            | 504                            | 454                                |
| Rest of Asia-Pacific   | 1,209                          | 1,047                          | 1,188                              |
| North America <sup>1</sup>   | 5,226                          | 3,638                          | 4,822                              |
| Latin America <sup>1</sup>   | 1,804                          | 1,346                          | 1,478                              |
|  | <u>14,567</u>                  | <u>12,313</u>                  | <u>13,800</u>                      |
| <b>Troubled debt restructurings</b>  |                                |                                |                                    |
| Europe   | 601                            | 293                            | 360                                |
| Hong Kong  | 162                            | 197                            | 189                                |
| Rest of Asia-Pacific   | 47                             | 91                             | 73                                 |
| North America <sup>1</sup>   | 2,232                          | 1,432                          | 1,712                              |
| Latin America <sup>1</sup>   | 796                            | 876                            | 915                                |
|  | <u>3,838</u>                   | <u>2,889</u>                   | <u>3,249</u>                       |
| <b>Unimpaired loans contractually past due 90 days or more as to principal or interest</b> |                                |                                |                                    |
| Europe   | 193                            | 364                            | 237                                |
| Hong Kong  | 58                             | 99                             | 79                                 |
| Rest of Asia-Pacific   | 135                            | 58                             | 78                                 |
| North America <sup>1</sup>   | 1,327                          | 1,083                          | 1,364                              |
| Latin America <sup>1</sup>   | 318                            |                                | 165                                |
|  | <u>2,031</u>                   | <u>1,604</u>                   | <u>1,923</u>                       |
| <b>Risk elements on loans</b>  |                                |                                |                                    |
| Europe   | 6,655                          | 6,435                          | 6,455                              |
| Hong Kong  | 687                            | 800                            | 722                                |
| Rest of Asia-Pacific   | 1,391                          | 1,196                          | 1,339                              |
| North America <sup>1</sup>   | 8,785                          | 6,153                          | 7,898                              |

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|  |               |               |               |
|--|---------------|---------------|---------------|
| Latin America <sup>1</sup>   | 2,918         | 2,222         | 2,558         |
|  | <u>20,436</u> | <u>16,806</u> | <u>18,972</u> |
| <b>Assets held for resale</b>  |               |               |               |
| Europe   | 48            | 47            | 30            |
| Hong Kong  | 28            | 58            | 42            |
| Rest of Asia-Pacific   | 16            | 3             | 17            |
| North America <sup>1</sup>   | 1,106         | 684           | 916           |
| Latin America <sup>1</sup>   | 93            | 47            | 91            |
|  | <u>1,291</u>  | <u>839</u>    | <u>1,096</u>  |
| <b>Total risk elements</b>   |               |               |               |
| Europe   | 6,703         | 6,482         | 6,485         |
| Hong Kong  | 715           | 858           | 764           |
| Rest of Asia-Pacific   | 1,407         | 1,199         | 1,356         |
| North America <sup>1</sup>   | 9,891         | 6,837         | 8,814         |
| Latin America <sup>1</sup>   | 3,011         | 2,269         | 2,649         |
|  | <u>21,727</u> | <u>17,645</u> | <u>20,068</u> |
|  | %             | %             | %             |
| Loan impairment allowances as a percentage of risk elements on loans | <u>70.1</u>   | <u>67.7</u>   | <u>71.6</u>   |

1 In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

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## Liquidity and funding management

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There have been no material changes to HSBC's objectives for the management of liquidity and funding risks as described in the *Annual Report and Accounts 2006*. The key features are repeated below.

Liquidity and funding risk is managed and monitored on a legal entity basis. It is HSBC's general policy that each banking entity should be self-sufficient with regard to funding its own operations.

Current accounts and savings deposits payable on demand or at short notice form a significant part of HSBC's funding. HSBC places considerable importance on maintaining the stability of these deposits. Stability depends upon preserving depositor confidence in HSBC's capital strength and liquidity, and on competitive and transparent deposit-pricing strategies.

HSBC also accesses professional markets in order to provide funding for non-banking subsidiaries that do not accept deposits, to maintain a presence in local money markets and to optimise the funding of asset maturities not naturally matched by core deposit funding. In aggregate, HSBC's banking entities are liquidity providers to the inter-bank market, placing significantly more funds with other banks than they borrow.

The main operating subsidiary that does not accept deposits is HSBC Finance, which funds itself principally by taking term funding in the professional markets and by securitising assets. At 30 June 2007, US\$144 billion (30 June 2006: US\$142 billion; 31 December 2006: US\$150 billion) of HSBC Finance's liabilities were drawn from professional markets, utilising a range of products, maturities and currencies to avoid undue reliance on any particular funding source.

Of total liabilities of US\$2,024 billion at 30 June 2007 (30 June 2006: US\$1,631 billion; 31 December 2006: US\$1,746 billion), funding from customers amounted to US\$981 billion (30 June 2006: US\$834 billion; 31 December 2006: US\$911 billion), of which US\$951 billion (30 June 2006: US\$808 billion; 31 December 2006: US\$872 billion) was contractually repayable within one year. However, although the contractual repayments of many customer accounts are on demand or at short notice, in practice short-term deposit balances remain stable as inflows and outflows broadly match.

### Ratio of net liquid assets to customer liabilities

A key measure used by the Group for managing liquidity risk is the ratio of net liquid assets to customer liabilities. Minimum liquidity ratio limits are set for each bank operating entity. Generally, liquid assets comprise cash balances, short-term interbank deposits and highly-rated debt securities available for immediate sale and for which a deep and liquid market exists. Net liquid assets are liquid assets less all wholesale market funds, and all funds provided by customers deemed to be professional, maturing in the next 30 days. The definition of a professional customer takes account of the size of the customer's total deposits.

Although consolidated data is not utilised in the management of HSBC's liquidity, the consolidated liquidity ratio figures of net liquid assets to customer liabilities shown in the following table provide a useful insight into the overall liquidity position of the Group's banking entities. The Group's liquidity risk has not changed materially during the period.

|               | Half-year to         |                      |                          |
|---------------|----------------------|----------------------|--------------------------|
|               | 30 June<br>2007<br>% | 30 June<br>2006<br>% | 31 December<br>2006<br>% |
| At period end | 19.4                 | 19.4                 | 20.6                     |
| Maximum       | 20.6                 | 20.9                 | 22.1                     |
| Minimum       | 18.6                 | 17.1                 | 18.1                     |
| Average       | 19.8                 | 18.8                 | 19.9                     |

## Market risk management

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The objective of HSBC's market risk management is to manage and control market risk exposures in order to optimise return on risk while maintaining a market profile consistent with the Group's status as a premier provider of financial products and services.

Market risk is the risk that movements in market risk factors, including foreign exchange rates and commodity prices, interest rates, credit spreads and equity prices will reduce HSBC's income or the value of its portfolios. Credit risk is discussed separately under [Credit risk management](#).

HSBC separates exposures to market risk into either trading or non-trading portfolios. Trading portfolios include those positions arising from market-making, proprietary position-taking and other marked-to-market positions so designated. The contribution of the marked-to-market positions so designated but not held with trading intent is disclosed separately.

Non-trading portfolios primarily arise from the interest rate management of HSBC's retail and commercial banking assets and liabilities.

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## The Management of Risk (continued)

### Value at risk ( VAR )

One of the principal tools used by HSBC to monitor and limit market risk exposure is VAR. VAR is a technique that estimates the potential losses that could occur on risk positions as a result of movements in market rates and prices over a specified time horizon and to a given level of confidence.

The VAR models used by HSBC are based predominantly on historical simulation. The historical simulation models derive plausible future scenarios from historical market rate time series, taking account of inter-relationships between different markets and rates, for example, between interest rates and foreign exchange rates. The models also incorporate the impact of option features in the underlying exposures.

The historical simulation models used by HSBC incorporate the following features:

- potential market movements are calculated with reference to data from the last two years;
- historical market rates and prices are calculated with reference to foreign exchange rates and commodity prices, interest rates, equity prices and the associated volatilities;
- VAR is calculated to a 99 per cent confidence level; and
- VAR is calculated for a one-day holding period.

HSBC routinely validates the accuracy of its VAR models by back-testing the actual daily profit and loss results, adjusted to remove non-modelled items such as fees and commissions, against the corresponding VAR numbers. Statistically, HSBC would expect to see losses in excess of VAR only one per cent of the time over a one-year holding period. The actual number of excesses over this period can therefore be used to gauge how well the models are performing.

Although a valuable guide to risk, VAR should always be viewed in the context of its limitations. For example:

- using historical data as a proxy for estimating future events may not encompass all potential events, particularly those which are extreme in nature;
- a 1-day holding period assumes that all positions can be liquidated or hedged in one day. This may not fully reflect the market risk arising at times of severe illiquidity, when a 1-day holding period may be insufficient to liquidate or hedge all positions fully;
- a 99 per cent confidence level, by definition, does not take into account losses that might occur beyond this level of confidence; and
- VAR is calculated on the basis of exposures outstanding at the close of business and therefore does not necessarily reflect intra-day exposures.

HSBC recognises these limitations by augmenting its VAR limits with other position and sensitivity limit structures. Additionally, HSBC applies a wide range of stress testing, both on individual portfolios and on the Group's consolidated positions. HSBC's stress-testing regime provides senior management with an assessment of the financial impact of identified extreme events on the market risk exposures of HSBC.

The VAR, for both trading and non-trading portfolios, for Global Markets was as follows:

Value at risk

Half-year to

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|               | <b>30 June<br/>2007<br/>US\$m</b> | 30 June<br>2006<br>US\$m | 31 December<br>2006<br>US\$m |
|---------------|-----------------------------------|--------------------------|------------------------------|
| At period end | <b>103.1</b>                      | 77.0                     | 67.3                         |
| Average       | <b>80.8</b>                       | 92.3                     | 56.6                         |
| Minimum       | <b>60.2</b>                       | 53.4                     | 39.4                         |
| Maximum       | <b>112.6</b>                      | 137.5                    | 80.1                         |

Average VAR for the first half of 2007 fell compared with the same period in the previous year. The major cause of this was a reduction in risk positions arising from the Group's balance sheet management activities.

The histograms overleaf illustrate the frequency of daily revenues arising from Global Markets business and other trading activities. The average daily revenue earned therefrom in the first half of 2007 was US\$26.3 million, compared with US\$22.3 million in the first half of 2006. The standard deviation of these daily revenues was US\$17.8 million compared with US\$11.7 million in the first half of 2006. The standard deviation measures the variation of daily revenues about the mean value of those revenues.

An analysis of the frequency distribution of daily revenues shows that there was one day with negative revenue during the first half of 2007 compared with no days in the first half of 2006. The most frequent result was daily revenues of between US\$20 million and US\$24 million with 29 occurrences.

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## Daily distribution of Global Markets trading, balance sheet management and other trading revenues

*Half-year to 30 June 2007*

■ Profit and loss frequency

*Half-year to 30 June 2006*

■ Profit and loss frequency

*Half-year to 31 December 2006*

■ Profit and loss frequency

## Fair value and price verification control

Where certain financial instruments are carried on the Group's balance sheet at fair value, the valuation and the related price verification processes are subject to independent validation across the Group. HSBC's policies and procedures are as described on page 218 in the *Annual Report and Accounts 2006*.

## Trading portfolios

HSBC's control of market risk is based on a policy of restricting individual operations to trading within a list of permissible instruments authorised for each site by Traded Credit and Market Risk, enforcing rigorous new product approval procedures, and restricting trading in the more complex derivative products to offices with appropriate levels of product expertise and robust control systems.

In addition, at both portfolio and position levels, market risk in trading portfolios is monitored and controlled using a complementary set of techniques. These include VAR and, for interest rate risk, present value of a basis point movement in interest rates, together with stress and sensitivity testing and concentration limits. These techniques quantify the effect on capital of defined market movements.

Total trading VAR for Global Markets at 30 June 2007 was US\$44.1 million. The VAR from positions taken without trading intent was US\$6.1 million, the principal components of which were hedges that failed to meet the strict documentation and testing requirements of IAS 39

Financial Instruments: Recognition and Measurement (i.e. non-qualifying hedges), and other positions transacted as economic hedges which also did not qualify for hedge accounting. HSBC's policy on hedging is to manage economic risk in the most appropriate way without regard as to whether hedge accounting is available and within limits regarding the potential volatility of reported earnings.

Trading VAR is further analysed below by risk type, by positions taken with trading intent and by positions taken without trading intent:



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HSBC HOLDINGS PLC

**The Management of Risk** (continued)

|   | <b>Foreign<br/>exchange<br/>and<br/>commodity<br/>US\$m</b> | <b>Interest<br/>rate<br/>US\$m</b> | <b>Equity<br/>US\$m</b> | <b>Total<br/>US\$m</b> |
|---|---|------------------------------------|-------------------------|------------------------|
| <b>Total trading VAR by risk type</b>                       |   |                                    |                         |                        |
| <b>At 30 June 2007</b>                                      | <b>10.0</b>   | <b>35.2</b>                        | <b>14.9</b>             | <b>44.1</b>            |
| At 30 June 2006   | 6.6   | 26.9                               | 5.7                     | 21.2                   |
| At 31 December 2006   | 7.3   | 26.0                               | 11.8                    | 32.6                   |
| <b>Average</b>  |   |                                    |                         |                        |
| <b>First half of 2007</b>                                   | <b>10.1</b>   | <b>30.5</b>                        | <b>12.3</b>             | <b>37.0</b>            |
| First half of 2006  | 6.4   | 37.9                               | 5.4                     | 36.7                   |
| Second half of 2006   | 6.2   | 30.0                               | 7.5                     | 30.1                   |
| <b>Minimum</b>  |   |                                    |                         |                        |
| <b>First half of 2007</b>                                   | <b>4.4</b>  | <b>24.5</b>                        | <b>8.1</b>              | <b>29.0</b>            |
| First half of 2006  | 3.7   | 24.1                               | 2.6                     | 21.2                   |
| Second half of 2006   | 2.6   | 18.3                               | 4.2                     | 20.9                   |
| <b>Maximum</b>  |   |                                    |                         |                        |
| <b>First half of 2007</b>                                   | <b>23.2</b>   | <b>38.5</b>                        | <b>16.9</b>             | <b>45.7</b>            |
| First half of 2006  | 12.7  | 53.6                               | 7.9                     | 52.3                   |
| Second half of 2006   | 11.9  | 43.8                               | 11.8                    | 42.7                   |
| <b>Positions taken with trading intent VAR by risk type</b> |   |                                    |                         |                        |
| <b>At 30 June 2007</b>                                      | <b>10.0</b>   | <b>31.5</b>                        | <b>14.9</b>             | <b>39.9</b>            |
| At 30 June 2006   | 6.6   | 24.5                               | 5.7                     | 19.9                   |
| At 31 December 2006   | 7.3   | 27.9                               | 11.8                    | 30.2                   |
| <b>Average</b>  |   |                                    |                         |                        |
| <b>First half of 2007</b>                                   | <b>10.1</b>   | <b>30.2</b>                        | <b>12.3</b>             | <b>36.5</b>            |
| First half of 2006  | 6.4   | 35.0                               | 5.4                     | 34.6                   |
| Second half of 2006   | 6.2   | 28.4                               | 7.5                     | 28.6                   |
| <b>Minimum</b>  |   |                                    |                         |                        |
| <b>First half of 2007</b>                                   | <b>4.4</b>  | <b>24.2</b>                        | <b>8.1</b>              | <b>30.1</b>            |
| First half of 2006  | 3.7   | 23.6                               | 2.6                     | 19.9                   |
| Second half of 2006   | 2.6   | 18.3                               | 4.2                     | 20.4                   |

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|                           |             |             |             |             |
|---------------------------|-------------|-------------|-------------|-------------|
| Maximum                   |             |             |             |             |
| <b>First half of 2007</b> | <b>23.2</b> | <b>38.1</b> | <b>16.9</b> | <b>45.1</b> |
| First half of 2006        | 12.7        | 49.6        | 7.9         | 48.2        |
| Second half of 2006       | 11.9        | 41.1        | 11.8        | 40.0        |

Positions taken without trading intent VAR by risk type

|                        |            |            |
|------------------------|------------|------------|
| <b>At 30 June 2007</b> | <b>6.1</b> | <b>6.1</b> |
| At 30 June 2006        | 4.6        | 4.6        |
| At 31 December 2006    | 4.7        | 4.7        |

Average

|                           |            |            |
|---------------------------|------------|------------|
| <b>First half of 2007</b> | <b>4.2</b> | <b>4.2</b> |
| First half of 2006        | 7.6        | 7.6        |
| Second half of 2006       | 3.7        | 3.7        |

Minimum

|                           |            |            |
|---------------------------|------------|------------|
| <b>First half of 2007</b> | <b>2.3</b> | <b>2.3</b> |
| First half of 2006        | 4.2        | 4.2        |
| Second half of 2006       | 2.5        | 2.5        |

Maximum

|                           |            |            |
|---------------------------|------------|------------|
| <b>First half of 2007</b> | <b>7.3</b> | <b>7.3</b> |
| First half of 2006        | 10.5       | 10.5       |
| Second half of 2006       | 7.9        | 7.9        |

[Back to Contents](#)**Non-trading portfolios**

The principal objective of market risk management of non-trading portfolios is to optimise net interest income.

Market risk in non-trading portfolios arises principally from mismatches between the future yield on assets and their funding cost, as a result of interest rate changes. Analysis of this risk is complicated by having to make assumptions on optionality in certain product areas, for example, mortgage prepayments, and from behavioural assumptions regarding the economic duration of liabilities which are contractually repayable on demand, for example, current accounts. The prospective change in future net interest income

from non-trading portfolios will be reflected in the current realisable value of these positions, should they be sold or closed prior to maturity. In order to manage this risk optimally, market risk in non-trading portfolios is transferred to Global Markets or to separate books managed under the supervision of the local Asset and Liability Committee ( ALCO ).

Once market risk has been consolidated in Global Markets or ALCO-managed books, the net exposure is typically managed through the use of interest rate swaps within agreed limits.

The principal non-trading risks which are not included in VAR for Global Markets (see Value at risk above) are detailed below.

## Non-trading risks not included in Global Markets VAR

|                           | <b>HSBC<br/>Finance<br/>US\$m</b> | <b>Mortgage<br/>servicing<br/>rights<br/>US\$m</b> | <b>Capital<br/>instruments<br/>US\$m</b> |
|---------------------------|-----------------------------------|--|--|
| <b>At 30 June 2007</b>    | <b>8.4</b>                        | <b>3.8</b>   | <b>80.6</b>                              |
| At 30 June 2006           | 8.1                               | 2.5  | 74.3                                     |
| At 31 December 2006       | 11.6                              | 3.2  | 87.4                                     |
| Average                   |                                   |  |  |
| <b>First half of 2007</b> | <b>8.5</b>                        | <b>3.3</b>   | <b>84.9</b>                              |
| First half of 2006        | 15.2                              | 3.0  | 65.8                                     |
| Second half of 2006       | 16.6                              | 2.9  | 78.5                                     |
| Minimum                   |                                   |  |  |
| <b>First half of 2007</b> | <b>5.9</b>                        | <b>2.8</b>   | <b>80.6</b>                              |
| First half of 2006        | 6.8                               | 2.5  | 58.8                                     |
| Second half of 2006       | 10.4                              | 2.5  | 72.9                                     |
| Maximum                   |                                   |  |  |
| <b>First half of 2007</b> | <b>11.8</b>                       | <b>3.9</b>   | <b>92.2</b>                              |
| First half of 2006        | 23.0                              | 3.9  | 74.3                                     |
| Second half of 2006       | 23.9                              | 3.5  | 87.4                                     |

The nature of non-trading market risks is explained on page 220 of the *Annual Report and Accounts 2006*.

Market risk arising in HSBC's insurance businesses is discussed in Risk management of insurance operations on page 120.

Market risk also arises within HSBC's defined benefit pension schemes to the extent that the obligations of the schemes are not fully matched by assets with determinable cash flows. The risk is that market movements in asset values could result in a portfolio of assets which are insufficient over time to cover the level of projected liabilities. The value of projected liabilities is driven by changes in discount rates, longevity and inflation. Management, together with the trustees who act on behalf of the pension scheme beneficiaries, assess the level of this

risk using reports prepared by independent external actuaries.

The present value of HSBC's defined benefit pension schemes' liabilities was US\$31.0 billion at 30 June 2007, compared with US\$32.2 billion at 31 December 2006 and US\$28.1 billion at 30 June 2006. Assets of the defined benefit pension schemes at 30 June 2007 comprised 26 per cent equity investments (31 December 2006: 30 per cent; 30 June 2006: 43 per cent); 62 per cent debt securities (31 December 2006: 56 per cent; 30 June 2006: 42 per cent) and 12 per cent other (including property) (31 December 2006: 14 per cent; 30 June 2006: 15 per cent).

#### **Sensitivity of net interest income**

There have been no material changes since 31 December 2006 to HSBC's measurement and

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HSBC HOLDINGS PLC

**The Management of Risk** (continued)

management of the sensitivity of net interest income to movements in interest rates.

A principal part of HSBC's management of market risk in non-trading portfolios is to monitor the sensitivity of projected net interest income under varying interest rate scenarios (simulation modelling). HSBC aims, through its management of market risk in non-trading portfolios, to mitigate the effect of prospective interest rate movements which could reduce future net interest income, while balancing the cost of such hedging activities on the current net revenue stream.

The table below sets out the impact on future net interest income of an incremental 25 basis points

parallel rise or fall in all yield curves worldwide at the beginning of each quarter during the 12 months from July 2007. Assuming no management actions, a series of such rises would decrease planned net interest income for the 12 months to 30 June 2008 by US\$656 million, while a series of such falls would increase planned net interest income by US\$615 million. These figures incorporate the effect of any option features in the underlying exposures.

Instead of assuming that all interest rates move together, HSBC groups its interest rate exposures into blocs of currencies whose interest rates are considered likely to move together. The sensitivity of projected net interest income, on this basis, is as follows:

## Sensitivity of projected net interest income

|  | US dollar<br>bloc<br>US\$m | Rest of<br>Americas<br>bloc<br>US\$m | Hong<br>Kong<br>dollar<br>bloc<br>US\$m | Rest of<br>Asia<br>bloc<br>US\$m | Sterling<br>bloc<br>US\$m | Euro<br>bloc<br>US\$m | Total<br>US\$m |
|--|----------------------------|--------------------------------------|---|----------------------------------|---------------------------|-----------------------|----------------|
| <b>Change in July 2007 to June 2008<br/>projected net interest income</b>        |                            |                                      |   |                                  |                           |                       |                |
| + 25 basis points shift in yield curves at the beginning of each quarter         | (352)                      | 40                                   | 2                                       | 55                               | (204)                     | (197)                 | (656)          |
| - 25 basis points shift in yield curves at the beginning of each quarter         | 287                        | (41)                                 | 17                                      | (34)                             | 199                       | 187                   | 615            |
| <b>Change in January 2007 to December<br/>2007 projected net interest income</b> |                            |                                      |   |                                  |                           |                       |                |
| + 25 basis points shift in yield curves at the beginning of each quarter         | (342)                      | 53                                   | (32)                                    | 18                               | (163)                     | (112)                 | (578)          |
| - 25 basis points shift in yield curves at the beginning of each quarter         | 249                        | (53)                                 | 52                                      | (14)                             | 164                       | 113                   | 511            |

The interest rate sensitivities set out in the table above are illustrative only and are based on simplified scenarios. The figures represent the effect on projected net interest income of the pro forma movements of the yield curve on the Group's current interest rate risk profile. This effect, however, does not incorporate actions that would be taken by Global Markets or in the business units to mitigate the impact of this interest rate

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risk. In reality, Global Markets seeks proactively to change the interest rate risk profile to minimise losses and optimise net revenues. The projections above also assume that interest rates of all maturities move by the same amount and, therefore, do not reflect the potential impact on net interest income of some rates changing while others remain unchanged. The projections make other simplifying assumptions too, including that all positions run to maturity.

HSBC's core exposure to the effect of movements in interest rates on its net interest income arise from three areas: core deposit franchises, HSBC Finance and Global Markets. This is described more fully in the *Annual Report and Accounts 2006*.

The major driver of the changes in projected net interest income from January 2007 to December 2007 and from July 2007 to June 2008 is growth in net trading assets, the funding for which is generally sourced from floating rate retail deposits and recorded in net interest income but the income from which is recorded in net trading income.

Projecting the movement in net interest income from prospective changes in interest rates is a complex interaction of structural and managed exposures. In a rising rate environment, the most critical exposures are those managed within Global Markets.

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## Sensitivity of reported reserves to interest rate movements

|   | <b>Impact in the preceding 6 months</b> |                          |                          |
|---|---|--------------------------|--------------------------|
|   | <b>US\$m</b>                            | <b>Maximum<br/>US\$m</b> | <b>Minimum<br/>US\$m</b> |
| <b>At 30 June 2007</b>                              |   |                          |                          |
| + 100 basis point parallel move in all yield curves | (1,713)                                 | (1,713)                  | (1,519)                  |
| As a percentage of total shareholders' equity       | (1.4%)                                  | (1.4%)                   | (1.3%)                   |
| 100 basis point parallel move in all yield curves   | 1,668                                   | 1,668                    | 1,430                    |
| As a percentage of total shareholders' equity       | 1.4%                                    | 1.4%                     | 1.2%                     |
| <b>At 30 June 2006</b>                              |   |                          |                          |
| + 100 basis point parallel move in all yield curves | (1,638)                                 | (2,010)                  | (1,638)                  |
| As a percentage of total shareholders' equity       | (1.6%)                                  | (2.0%)                   | (1.6%)                   |
| 100 basis point parallel move in all yield curves   | 1,615                                   | 1,944                    | 1,615                    |
| As a percentage of total shareholders' equity       | 1.6%                                    | 1.9%                     | 1.6%                     |
| <b>At 31 December 2006</b>                          |   |                          |                          |
| + 100 basis point parallel move in all yield curves | (1,558)                                 | (1,558)                  | (1,358)                  |
| As a percentage of total shareholders' equity       | (1.4%)                                  | (1.4%)                   | (1.3%)                   |
| 100 basis point parallel move in all yield curves   | 1,456                                   | 1,456                    | 1,270                    |
| As a percentage of total shareholders' equity       | 1.3%                                    | 1.3%                     | 1.2%                     |

The sensitivity of reported reserves to interest rate movements as at 30 June 2007, and the maximum and minimum month figure during the period, are shown in the above table. These sensitivities are illustrative only and are based on simplified scenarios. The table shows interest rate risk exposures arising in available-for-sale portfolios and from cash flow hedges which are marked-to-market through reserves. These particular exposures form only a part of the Group's overall interest rate exposures. The accounting treatment under IFRSs of the Group's remaining interest rate exposures, while economically largely offsetting the exposures shown in the above table, does not require revaluation movements to go to reserves.

**Structural foreign exchange exposures**

Structural foreign exchange exposures represent net investments in subsidiaries, branches or associates, the functional currencies of which are currencies other than the US dollar. HSBC's policies and procedures for managing these exposures are as described in the *Annual Report and Accounts 2006*.

**Operational risk management**

Operational risk is the risk of loss arising from fraud, unauthorised activities, error, omission, inefficiency, systems failure or external events. It is inherent in every business organisation and covers a wide spectrum of issues.

There have been no material changes to HSBC's approach to and management of operational risk as described in the *Annual Report and Accounts 2006*. The overall operational risk management framework

and local management responsibilities are summarised below.

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HSBC has codified its operational risk management process by issuing a high level Standard, supplemented by more detailed formal guidance. This explains how HSBC manages operational risk by identifying, assessing, monitoring, controlling and mitigating the risk, rectifying operational risk events, and implementing any additional procedures required for compliance with local regulatory requirements. The processes undertaken to manage operational risk are determined by reference to the scale and nature of each HSBC operation.

In each of HSBC's subsidiaries, local management is responsible for implementing HSBC's standards on operational risk throughout their operations and, where deficiencies are evident, rectifying them within a reasonable timeframe. Subsidiaries acquired by HSBC are required to assess, plan and implement the Standard's requirements within an agreed timescale.

### **Legal risk management**

Each operating company is required to implement policies, procedures and guidelines in respect of the management and control of legal risk which conform to HSBC standards. Legal risk falls within the definition of operational risk and includes contractual risk, legislative risk, intellectual property risk and litigation risk. Litigation risk is the risk of:

- failing to act appropriately in response to a claim made against any HSBC company; or



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HSBC HOLDINGS PLC

## The Management of Risk (continued)

- being unable to defend successfully a claim brought against any HSBC company; or
- HSBC being unable to take action to enforce its rights through the courts.

HSBC has a global legal function dedicated to managing legal risk in accordance with policies and procedures as described in the *Annual Report and Accounts 2006*.

### Reputational risk management

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The safeguarding of HSBC's reputation is of paramount importance to its continued prosperity and is the responsibility of every member of staff. Reputational risks can arise from social, ethical or environmental issues, or as a consequence of operational risk events. As a banking group, HSBC's good 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.

HSBC's management of reputational risk is described in the *Annual Report and Accounts 2006*.

### Risk management of insurance operations

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Within its service proposition, HSBC offers its customers a wide range of insurance products. Both life and non-life insurance are underwritten, principally in the UK, Hong Kong, Mexico, Brazil, the US and Argentina.

Life insurance contracts include participating business (with discretionary participation features) such as endowments and pensions, credit life business in respect of income and payment protection, annuities, term assurance and critical illness covers.

Non-life insurance contracts include motor, fire and other damage, accident and health, repayment protection and commercial and liability business.

The principal insurance risk faced by HSBC is that the cost of claims combined with acquisition costs may exceed the aggregate amount of premiums received and investment income.

HSBC manages insurance risks through the application of formal underwriting, reinsurance and claims procedures designed to ensure compliance with regulations, by diversifying insurance business by type and geography, and by focusing on risks that are straightforward to manage (those which, in the main, are related to core underlying banking activities such as credit life products). The following tables provide an analysis of the insurance risk exposures by geography and by type of business, and demonstrate the Group's diversification of risk. For example, personal lines tend to be higher volume and of lower individual value than commercial lines. Life business tends to be longer term in nature than non-life business and frequently involves an element of savings and investment in the contract. Separate tables are therefore presented for life and non-life businesses, reflecting their very distinct risk characteristics. The life insurance risk table provides an analysis of insurance liabilities as the best available overall measure of insurance exposure. The table for non-life business uses written premiums as representing the best available measure of risk exposure.

HSBC's management of insurance risk, including the risks relating to different life and non-life products, is described in the *Annual Report and Accounts 2006*.

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Analysis of life insurance risk liabilities to policyholders

|  | Europe<br>US\$m | Hong<br>Kong<br>US\$m | Rest of<br>Asia-<br>Pacific<br>US\$m | North<br>America<br>US\$m | Latin<br>America<br>US\$m | Total<br>US\$m |
|--|-----------------|-----------------------|--------------------------------------|---------------------------|---------------------------|----------------|
| <b>At 30 June 2007</b>                       |                 |                       |                                      |                           |                           |                |
| Life (non-linked)                            |                 |                       |                                      |                           |                           |                |
| Insurance contracts with DPF <sup>1</sup>    | 844             | 7,173                 | 201                                  |                           |                           | 8,218          |
| Credit life                                  | 234             |                       |                                      | 201                       |                           | 435            |
| Annuities                                    | 310             |                       | 26                                   | 1,210                     | 1,480                     | 3,026          |
| Term assurance and other long-term contracts | 94              | 76                    | 93                                   |                           | 291                       | 554            |
|  | <u>1,482</u>    | <u>7,249</u>          | <u>320</u>                           | <u>1,411</u>              | <u>1,771</u>              | <u>12,233</u>  |
| Total life (non-linked)                      | 1,482           | 7,249                 | 320                                  | 1,411                     | 1,771                     | 12,233         |
| Life (linked)                                | 1,693           | 1,058                 | 426                                  |                           | 1,677                     | 4,854          |
| Investment contracts with DPF <sup>1</sup>   | 17,100          |                       | 22                                   |                           |                           | 17,122         |
|  | <u>20,275</u>   | <u>8,307</u>          | <u>768</u>                           | <u>1,411</u>              | <u>3,448</u>              | <u>34,209</u>  |
| Insurance liabilities to policyholders       | 20,275          | 8,307                 | 768                                  | 1,411                     | 3,448                     | 34,209         |

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|   | Europe<br>US\$m | Hong<br>Kong<br>US\$m | Rest of<br>Asia-<br>Pacific<br>US\$m | North<br>America<br>US\$m | Latin<br>America<br>US\$m | Total<br>US\$m |
|---|-----------------|-----------------------|--------------------------------------|---------------------------|---------------------------|----------------|
| At 30 June 2006 (restated2)                   |                 |                       |                                      |                           |                           |                |
| Life (non-linked)                             |                 |                       |                                      |                           |                           |                |
| Insurance contracts with DPF <sup>1</sup>     | 181             | 4,774                 | 163                                  |                           |                           | 5,118          |
| Credit life                                   | 189             |                       |                                      | 183                       |                           | 372            |
| Annuities                                     | 219             |                       | 23                                   | 1,138                     | 1,130                     | 2,510          |
| Term assurance and other long-term contracts  | 1,077           | 75                    | 85                                   |                           | 273                       | 1,510          |
| <b>Total life (non-linked)</b>                | <b>1,666</b>    | <b>4,849</b>          | <b>271</b>                           | <b>1,321</b>              | <b>1,403</b>              | <b>9,510</b>   |
| Life (linked)                                 | 1,232           | 676                   | 345                                  |                           | 1,043                     | 3,296          |
| Investment contracts with DPF <sup>1</sup>    |                 |                       | 15                                   |                           |                           | 15             |
| <b>Insurance liabilities to policyholders</b> | <b>2,898</b>    | <b>5,525</b>          | <b>631</b>                           | <b>1,321</b>              | <b>2,446</b>              | <b>12,821</b>  |
| At 31 December 2006                           |                 |                       |                                      |                           |                           |                |
| Life (non-linked)                             |                 |                       |                                      |                           |                           |                |
| Insurance contracts with DPF <sup>1</sup>     | 195             | 6,001                 | 193                                  |                           |                           | 6,389          |
| Credit life                                   | 130             |                       |                                      | 200                       |                           | 330            |
| Annuities                                     | 271             |                       | 26                                   | 1,106                     | 1,370                     | 2,773          |
| Term assurance and other long-term contracts  | 1,134           | 75                    | 89                                   |                           | 236                       | 1,534          |
| <b>Total life (non-linked)</b>                | <b>1,730</b>    | <b>6,076</b>          | <b>308</b>                           | <b>1,306</b>              | <b>1,606</b>              | <b>11,026</b>  |
| Life (linked)                                 | 1,270           | 765                   | 402                                  |                           | 1,248                     | 3,685          |
| Investment contracts with DPF <sup>1</sup>    |                 |                       | 20                                   |                           |                           | 20             |
| <b>Insurance liabilities to policyholders</b> | <b>3,000</b>    | <b>6,841</b>          | <b>730</b>                           | <b>1,306</b>              | <b>2,854</b>              | <b>14,731</b>  |

1 Insurance contracts and investment contracts with discretionary participation features ( DPF ) give policyholders the contractual right to receive, as a supplement to their guaranteed benefits, additional benefits that may be a significant portion of the total contractual benefits, but whose amount and timing is determined by HSBC. These additional benefits are contractually based on the performance of a specified pool of contracts or assets, or the profit of the company issuing the contracts. The increase in investment contracts with DPF results from the acquisition of the remaining 50.01 per cent share in Erisa, the French insurance business, that the Group did not already own, in March 2007.

2 In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. The information as at 30 June 2006 has been restated accordingly.

Analysis of non-life insurance risk net written insurance premiums

|                                    | Europe<br>US\$m | Hong<br>Kong<br>US\$m | Rest of<br>Asia-<br>Pacific<br>US\$m | North<br>America<br>US\$m | Latin<br>America<br>US\$m | Total<br>US\$m |
|------------------------------------|-----------------|-----------------------|--------------------------------------|---------------------------|---------------------------|----------------|
| <b>Half-year to 30 June 2007</b>   |                 |                       |                                      |                           |                           |                |
| Accident and health                | 18              | 68                    | 2                                    |                           | 8                         | 96             |
| Motor                              | 172             | 8                     | 5                                    |                           | 96                        | 281            |
| Fire and other damage              | 99              | 11                    | 2                                    | 1                         | 6                         | 119            |
| Liability                          |                 | 9                     | 2                                    | 8                         | 15                        | 34             |
| Credit (non-life)                  | 125             |                       |                                      | 90                        |                           | 215            |
| Marine, aviation and transport     |                 | 6                     | 2                                    |                           | 8                         | 16             |
| Other non-life insurance contracts | 24              | 11                    |                                      | 6                         | 8                         | 49             |

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|                                       |            |            |           |            |            |            |
|---------------------------------------|------------|------------|-----------|------------|------------|------------|
| Total net written insurance premiums  | <b>438</b> | <b>113</b> | <b>13</b> | <b>105</b> | <b>141</b> | <b>810</b> |
| Half-year to 30 June 2006 (restated2) |            |            |           |            |            |            |
| Accident and health                   | 15         | 55         | 2         |            | 5          | 77         |
| Motor                                 | 93         | 9          | 7         |            | 77         | 186        |
| Fire and other damage                 | 113        | 16         | 2         |            | 5          | 136        |
| Liability                             |            | 11         | 1         |            | 10         | 22         |
| Credit (non-life)                     | 147        |            |           | 82         |            | 229        |
| Marine, aviation and transport        |            | 6          | 2         |            | 7          | 15         |
| Other non-life insurance contracts    |            | 11         |           |            | 7          | 18         |
| Total net written insurance premiums  | 368        | 108        | 14        | 82         | 111        | 683        |

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**The Management of Risk** (continued)

|   | Europe<br>US\$m | Hong<br>Kong<br>US\$m | Rest of<br>Asia-<br>Pacific<br>US\$m | North<br>America<br>US\$m | Latin<br>America<br>US\$m | Total<br>US\$m |
|---|-----------------|-----------------------|--------------------------------------|---------------------------|---------------------------|----------------|
| Half-year to 31 December 2006               |                 |                       |                                      |                           |                           |                |
| Accident and health                         | 11              | 42                    | 3                                    |                           | 5                         | 61             |
| Motor                                       | 92              | 6                     | 6                                    |                           | 80                        | 184            |
| Fire and other damage                       | 108             | 6                     | 3                                    | 2                         | 4                         | 123            |
| Liability                                   | 1               | 2                     | 1                                    | 8                         | 14                        | 26             |
| Credit (non-life)                           | 117             |                       |                                      | 91                        |                           | 208            |
| Marine, aviation and transport              | 1               | 5                     | 1                                    |                           | 5                         | 12             |
| Other non-life insurance contracts          | 13              | 13                    |                                      | 37                        | 13                        | 76             |
| <b>Total net written insurance premiums</b> | <b>343</b>      | <b>74</b>             | <b>14</b>                            | <b>138</b>                | <b>121</b>                | <b>690</b>     |

1 *Net written insurance premiums represent gross written premiums less gross written premiums ceded to reinsurers.*

2 *In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. The information as at 30 June 2006 has been restated accordingly.*

**Balance sheet of insurance operations by type of contract**

A key aspect of insurance risk management, in particular in the life insurance business, is the need to manage financial assets and their associated liabilities. Models which assess the effect on values under a range of future stress tests are used by local management to determine how the assets and liabilities should be matched. Of particular importance for a number of lines of business, such as annuities, is the need to match the pattern of expected cash flows, which in some cases can extend for many years.

The following table shows the composition of assets and liabilities and demonstrates that there was an appropriate level of matching. It may not always be possible to achieve complete matching of asset and liability durations, partly because there is uncertainty over the receipt of all future premiums and partly because the duration of liabilities may exceed the duration of the longest available dated fixed interest investments.

The total liabilities for insurance manufacturing operations at 30 June 2007 were US\$57 billion (30 June 2006: US\$30 billion; 31 December 2006: US\$34 billion), representing 3 per cent (30 June 2006 and 31 December 2006: 2 per cent) of the total liabilities included in HSBC's consolidated balance

sheet. This was an increase of 90 per cent compared with insurance liabilities at 30 June 2006 and 68 per cent at 31 December 2006. The increase was driven by the inclusion of Erisa, following HSBC's acquisition of the remaining shares in the company earlier this year. Erisa contributed US\$20 billion to the total insurance liabilities at 30 June 2007.

HSBC's business focus is on life insurance and, accordingly, 86 per cent of the total insurance manufacturing liabilities relate to life insurance contracts. The nature of the contracts is reflected in the level of insurance liabilities. Non-life insurance liabilities are predominantly set based on claims notified to the insurer and typically reflect the one year period of cover. For life contracts, a liability is established at the inception of the contract to reflect the expected claims over the life of the contract, which can span several years.

Excluding the impact of the inclusion of Erisa, the underlying growth in liabilities was US\$2.6 billion since 31 December 2006. This growth was driven by sales of life contracts in Hong Kong (US\$1.6 billion), the UK (US\$1.3 billion) and Latin America (US\$0.6 billion). This new business growth was partly offset by a US\$0.9 billion reduction in insurance liabilities in the UK, reflecting changes in FSA rules covering the calculation of actuarial liabilities on these contracts.



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## Balance sheet of insurance operations by type of contract

|  | Insurance contracts                            |                          |                    |   |                   | Investment contracts                           |                          |                |                                       |               | Total<br>US\$m |
|--|--|--------------------------|--------------------|---|-------------------|--|--------------------------|----------------|---------------------------------------|---------------|----------------|
|  | Contracts<br>with<br>DPF <sup>1</sup><br>US\$m | Unit-<br>linked<br>US\$m | Annuities<br>US\$m | Term<br>assurance <sup>2</sup><br>US\$m | Non-life<br>US\$m | Contracts<br>with<br>DPF <sup>3</sup><br>US\$m | Unit-<br>linked<br>US\$m | Other<br>US\$m | Other<br>assets <sup>4</sup><br>US\$m |               |                |
| <b>At 30 June 2007</b>   |  |                          |                    |   |                   |  |                          |                |                                       |               |                |
| Financial assets:  |  |                          |                    |   |                   |  |                          |                |                                       |               |                |
| trading assets   |  |                          | 46                 |   | 41                |  |                          |                | 33                                    | 120           |                |
| financial assets<br>designated at fair value                           | 1,851  | 4,138                    | 559                | 693                                     | 44                | 6,792  | 11,094                   | 1,610          | 2,686                                 | 29,467        |                |
| derivatives  |  | 349                      |                    |   | 1                 | 56   | 352                      | 3              |                                       | 761           |                |
| financial investments  | 4,949  |                          | 1,253              | 388                                     | 1,294             | 10,076   |                          | 1,412          | 2,712                                 | 22,084        |                |
| other financial assets   | 1,504  | 304                      | 419                | 197                                     | 704               | 616  | 409                      | 633            | 1,236                                 | 6,022         |                |
| <b>Total financial assets</b>  | <b>8,304</b>                                   | <b>4,791</b>             | <b>2,277</b>       | <b>1,278</b>                            | <b>2,084</b>      | <b>17,540</b>                                  | <b>11,855</b>            | <b>3,658</b>   | <b>6,667</b>                          | <b>58,454</b> |                |
| Reinsurance assets   | 1  | 62                       | 314                | 260                                     | 628               |  |                          |                | 54                                    | 1,319         |                |
| PVIF   |  |                          |                    |   |                   |  |                          |                | 1,909                                 | 1,909         |                |
| Other assets and investment<br>properties                              | 37   | 6                        | 574                | 124                                     | 174               | 97   | 68                       |                | 1,357                                 | 2,437         |                |
| <b>Total assets</b>  | <b>8,342</b>                                   | <b>4,859</b>             | <b>3,165</b>       | <b>1,662</b>                            | <b>2,886</b>      | <b>17,637</b>                                  | <b>11,923</b>            | <b>3,658</b>   | <b>9,987</b>                          | <b>64,119</b> |                |
| Liabilities under investment<br>contracts designated at fair<br>value  |  |                          |                    |   |                   |  |                          |                |                                       |               |                |
|  |  |                          |                    |   |                   |  | 11,132                   | 3,389          |                                       | 14,521        |                |
| Liabilities under investment<br>contracts carried at<br>amortised cost |  |                          |                    |   |                   |  |                          |                |                                       |               |                |
|  |  |                          |                    |   |                   |  |                          | 268            |                                       | 268           |                |
| Liabilities under insurance<br>contracts                               | 8,218  | 4,854                    | 3,026              | 989                                     | 2,720             | 17,122   |                          |                |                                       | 36,929        |                |
| Deferred tax   |  |                          |                    |   |                   |  |                          |                | 603                                   | 603           |                |
| Other liabilities  |  |                          |                    |   |                   |  |                          |                | 4,442                                 | 4,442         |                |
| <b>Total liabilities</b>   | <b>8,218</b>                                   | <b>4,854</b>             | <b>3,026</b>       | <b>989</b>                              | <b>2,720</b>      | <b>17,122</b>                                  | <b>11,132</b>            | <b>3,657</b>   | <b>5,045</b>                          | <b>56,763</b> |                |
| Shareholders' equity   |  |                          |                    |   |                   |  |                          |                | 7,356                                 | 7,356         |                |
| <b>Total liabilities and<br/>shareholders' equity</b>                  | <b>8,218</b>                                   | <b>4,854</b>             | <b>3,026</b>       | <b>989</b>                              | <b>2,720</b>      | <b>17,122</b>                                  | <b>11,132</b>            | <b>3,657</b>   | <b>12,401</b>                         | <b>64,119</b> |                |

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**The Management of Risk** (continued)

|   | Insurance contracts                            |                          |                    |   |                   | Investment contracts     |                |                                       | Total<br>US\$m |
|---|--|--------------------------|--------------------|---|-------------------|--------------------------|----------------|---------------------------------------|----------------|
|   | Contracts<br>with<br>DPF <sup>1</sup><br>US\$m | Unit-<br>linked<br>US\$m | Annuities<br>US\$m | Term<br>assurance <sup>2</sup><br>US\$m | Non-life<br>US\$m | Unit-<br>linked<br>US\$m | Other<br>US\$m | Other<br>assets <sup>4</sup><br>US\$m |                |
| At 30 June 2006   |  |                          |                    |   |                   |                          |                |                                       |                |
| Financial assets:   |  |                          |                    |   |                   |                          |                |                                       |                |
| trading assets  |  |                          |                    |   |                   |                          |                | 212                                   | 212            |
| financial assets designated at fair value                           | 927  | 2,525                    | 133                | 930                                     | 13                | 8,038                    | 1,519          | 1,608                                 | 15,693         |
| derivatives   | 64   | 436                      |                    |   |                   | 372                      | 4              |                                       | 876            |
| financial investments   | 2,731  |                          | 1,608              | 189                                     | 1,179             |                          | 1,617          | 2,141                                 | 9,465          |
| other financial assets  | 1,506  | 275                      | 419                | 416                                     | 659               | 264                      | 289            | 1,112                                 | 4,940          |
| Total financial assets  | 5,228  | 3,236                    | 2,160              | 1,535                                   | 1,851             | 8,674                    | 3,429          | 5,073                                 | 31,186         |
| Reinsurance assets  | 1  | 74                       | 214                | 658                                     | 620               |                          |                | 44                                    | 1,611          |
| PVIF  |  |                          |                    |   |                   |                          |                | 1,515                                 | 1,515          |
| Other assets and investment properties                              | 38   |                          | 115                | 43                                      | 390               |                          |                | 954                                   | 1,540          |
| Total assets  | 5,267  | 3,310                    | 2,489              | 2,236                                   | 2,861             | 8,674                    | 3,429          | 7,586                                 | 35,852         |
| Liabilities under investment contracts<br>designated at fair value  |  |                          |                    |   |                   | 8,538                    | 3,178          |                                       | 11,716         |
| Liabilities under investment contracts carried<br>at amortised cost |  |                          |                    |   |                   |                          | 188            |                                       | 188            |
| Liabilities under insurance contracts                               | 5,133  | 3,296                    | 2,510              | 1,882                                   | 2,842             |                          |                |                                       | 15,663         |
| Deferred tax  |  |                          |                    |   |                   |                          |                | 363                                   | 363            |
| Other liabilities   |  |                          |                    |   |                   |                          |                | 2,456                                 | 2,456          |
| Total liabilities   | 5,133  | 3,296                    | 2,510              | 1,882                                   | 2,842             | 8,538                    | 3,366          | 2,819                                 | 30,386         |
| Shareholders' equity  |  |                          |                    |   |                   |                          |                | 5,466                                 | 5,466          |
| Total liabilities and shareholders' equity                          | 5,133  | 3,296                    | 2,510              | 1,882                                   | 2,842             | 8,538                    | 3,366          | 8,285                                 | 35,852         |

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|  | Insurance contracts        |                   |                 |                                   |                | Investment contracts |              |                                 | Total US\$m   |
|--|----------------------------|-------------------|-----------------|-----------------------------------|----------------|----------------------|--------------|---------------------------------|---------------|
|  | Contracts with DPF 1 US\$m | Unit-linked US\$m | Annuities US\$m | Term assurance <sup>2</sup> US\$m | Non-life US\$m | Unit-linked US\$m    | Other US\$m  | Other assets <sup>4</sup> US\$m |               |
| At 31 December 2006  |                            |                   |                 |                                   |                |                      |              |                                 |               |
| Financial assets:  |                            |                   |                 |                                   |                |                      |              |                                 |               |
| trading assets   |                            |                   |                 |                                   | 117            |                      |              | 39                              | 156           |
| financial assets designated at fair value                        | 1,418                      | 2,998             | 366             | 950                               | 94             | 10,041               | 1,597        | 974                             | 18,438        |
| derivatives  | 96                         | 417               |                 |                                   |                | 363                  | 3            |                                 | 879           |
| financial investments  | 3,842                      |                   | 1,223           | 390                               | 1,554          |                      | 1,441        | 2,173                           | 10,623        |
| other financial assets   | 794                        | 52                | 719             | 138                               | 712            | 222                  | 428          | 632                             | 3,697         |
| <b>Total financial assets</b>                                    | <b>6,150</b>               | <b>3,467</b>      | <b>2,308</b>    | <b>1,478</b>                      | <b>2,477</b>   | <b>10,626</b>        | <b>3,469</b> | <b>3,818</b>                    | <b>33,793</b> |
| Reinsurance assets   | 2                          | 58                | 271             | 773                               | 665            |                      |              | 48                              | 1,817         |
| PVIF   |                            |                   |                 |                                   |                |                      |              | 1,549                           | 1,549         |
| Other assets and investment properties                           | 538                        | 203               | 395             | 356                               | 215            | 154                  | 204          | 614                             | 2,679         |
| <b>Total assets</b>  | <b>6,690</b>               | <b>3,728</b>      | <b>2,974</b>    | <b>2,607</b>                      | <b>3,357</b>   | <b>10,780</b>        | <b>3,673</b> | <b>6,029</b>                    | <b>39,838</b> |
| Liabilities under investment contracts designated at fair value  |                            |                   |                 |                                   |                |                      |              |                                 |               |
| Liabilities under investment contracts carried at amortised cost |                            |                   |                 |                                   |                |                      | 216          |                                 | 216           |
| Liabilities under insurance contracts                            | 6,389                      | 3,685             | 2,773           | 1,864                             | 2,939          |                      | 20           |                                 | 17,670        |
| Deferred tax   |                            |                   |                 |                                   |                |                      |              | 403                             | 403           |
| Other liabilities  |                            |                   |                 |                                   |                |                      |              | 2,322                           | 2,322         |
| <b>Total liabilities</b>   | <b>6,389</b>               | <b>3,685</b>      | <b>2,773</b>    | <b>1,864</b>                      | <b>2,939</b>   | <b>10,003</b>        | <b>3,511</b> | <b>2,725</b>                    | <b>33,889</b> |
| Shareholders' equity   |                            |                   |                 |                                   |                |                      |              | 5,949                           | 5,949         |
| <b>Total liabilities and shareholders' equity<sup>6</sup></b>    | <b>6,389</b>               | <b>3,685</b>      | <b>2,773</b>    | <b>1,864</b>                      | <b>2,939</b>   | <b>10,003</b>        | <b>3,511</b> | <b>8,674</b>                    | <b>39,838</b> |

1 Discretionary participation features.

2 Term assurance includes credit life insurance.

3 New category disclosed following HSBC's acquisition of the remaining 50.01 per cent of Erisa.

4 Other assets comprise solvency and unencumbered assets.

5 Excludes assets, liabilities and shareholders' funds of associate insurance company, Ping An Insurance.

6 Excludes assets, liabilities and shareholders' funds of associate insurance companies, Erisa and Ping An Insurance.

## Capital management and allocation

### Capital management

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It is HSBC's policy to maintain a strong capital base to support the development of its business. HSBC seeks to maintain a prudent balance between the different components of its capital and, in HSBC Holdings, between the composition of its capital and that of its investment in subsidiaries. Capital generated in excess of planned requirements is returned to HSBC Holdings, normally by way of dividends, and represents a source of strength for HSBC.

HSBC's capital management policy is described in further detail in the *Annual Report and Accounts 2006*.

### **Capital measurement and allocation**

The FSA supervises HSBC on a consolidated basis and, as such, receives information on the capital adequacy of, and sets capital requirements for, HSBC as a whole. Individual banking subsidiaries are directly regulated by their local banking supervisors, who set and monitor their capital adequacy requirements. In most jurisdictions, non-banking financial subsidiaries are also subject to the supervision and capital requirements of local regulatory authorities.

Further details regarding these requirements, including the constituent components of HSBC's capital base and the various regulatory limits which apply to them, and the categorisation of banking operations as trading or banking book for determining risk weighted assets, are detailed in the *Annual Report and Accounts 2006*. Changes to the definition of capital came into force on 1 January

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**The Management of Risk** (continued)

2007. They include the introduction of proportional consolidation of banking associates, which previously were either fully consolidated or deducted from capital, the relaxation of rules covering the deduction of investments in other banks' capital, and a change to make certain deductions, previously from total capital, now 50 per cent from each of tier 1 and tier 2 capital in the published disclosures. This applies to deductions of investments in insurance subsidiaries and associates, but the FSA has granted a transitional provision, until 31 December 2012, under which any of these insurance investments that were acquired before 20 July 2006 may be deducted from total capital instead. HSBC has elected to apply this transitional provision. HSBC complied with the FSA's capital adequacy requirements throughout 2006 and the first half of 2007.

**Basel II**

The Basel Committee on Banking Supervision has introduced a new framework for calculating minimum capital requirements. Known as Basel II, it replaces the 1988 Basel Capital Accord (Basel I). Basel II is structured around three pillars: minimum capital requirements, supervisory review process and market discipline. The supervisory objectives of Basel II are to promote safety and soundness in the financial system and maintain at least the current overall level of capital, enhance competitive equality, constitute a more comprehensive approach to addressing risks, and focus on internationally active banks.

The EU Capital Requirements Directive (CRD) recast the Banking Consolidation Directive and the Capital Adequacy Directive and is the means by which Basel II is implemented in the EU. The CRD required EU member states to bring implementing provisions into force on 1 January 2007, although in the case of the provisions relating to the calculation of minimum capital requirements, implementation may be delayed until 1 January 2008.

In October 2006, the FSA published the General Prudential Sourcebook (GENPRU) and the Prudential Sourcebook for Banks, Building Societies and Investment Firms (BIPRU), which took effect from 1 January 2007 and implemented the CRD in the UK. GENPRU introduced changes to the definition of capital and the methodology for calculating a firm's capital resources requirements.

BIPRU introduced the Basel II requirements for the calculation of risk weighted assets as well as changes to the consolidation regime, the trading book definition and various ancillary matters. Transitional provisions regarding the implementation of capital requirement calculations mean that, in general, unless firms notify the FSA to the contrary, they continue to apply existing capital requirement calculations until 1 January 2008.

**Future developments**

For credit risk, HSBC plans to adopt the internal ratings-based (IRB) advanced approach to Basel II for the majority of its businesses with effect from 1 January 2008, with the remainder on either IRB foundation or standardised approaches. These plans remain subject to regulatory approval. A rollout plan is in place to extend coverage of the advanced approach over the next three years, leaving a small residue of exposures on the standardised approach. HSBC will adopt the standardised approach for operational risk. For individual banking subsidiaries, the timing and manner of implementing Basel II varies by jurisdiction according to requirements set by local banking supervisors. Applying Basel II across HSBC's geographically diverse businesses, which operate in many different regulatory environments, presents a significant logistical and technological challenge, and an extensive programme of implementation projects is currently in progress.

Basel II allows local regulators to exercise discretion in a number of areas. The extent to which their requirements diverge, coupled with how the FSA and the local regulators in the other countries in which HSBC operates interact, will be key factors in completing implementation of Basel II. One example of regulatory uncertainty relates to the US, where no final rule has been issued (further detailed in the *Annual Report and Accounts 2006*). On 20 July 2007, the US Banking Agencies issued a joint press release announcing that they have reached an agreement regarding the implementation of Basel II in the US. This agreement is expected to lead to the finalisation of a rule implementing the advanced approaches which will be applicable to HSBC's North American operations. Uncertainty remains about its timing and content, but the press release indicated that the agencies have agreed that it should be finalised expeditiously. Notwithstanding these uncertainties, HSBC continues to assess the effect of Basel II on its reported capital adequacy.



[Back to Contents](#)**Source and application of tier 1 capital**

|   | Half-year to             |                          |                                 |
|---|--------------------------|--------------------------|---------------------------------|
|   | 30 June<br>2007<br>US\$m | 30 June<br>2006<br>US\$m | 31<br>December<br>2006<br>US\$m |
| <b>Movement in tier 1 capital</b>                                       |                          |                          |                                 |
| Opening tier 1 capital  | 87,842                   | 74,403                   | 82,138                          |
| Consolidated profits attributable to shareholders of the parent company | 10,895                   | 8,729                    | 7,060                           |
| Dividends   | (6,192)                  | (5,270)                  | (3,499)                         |
| Shares issued in lieu of dividends                                      | 2,826                    | 1,790                    | 735                             |
| Increase in goodwill and intangible assets deducted                     | (1,058)                  | (1,171)                  | (2,497)                         |
| Ordinary shares issued  | 118                      | 414                      | 601                             |
| Other (including exchange differences)                                  | 2,913                    | 3,243                    | 3,304                           |
| Closing tier 1 capital  | 97,344                   | 82,138                   | 87,842                          |
| <b>Movement in risk-weighted assets</b>                                 |                          |                          |                                 |
| Opening risk-weighted assets  | 938,678                  | 827,164                  | 872,893                         |
| Movements   | 102,862                  | 45,729                   | 65,785                          |
| Closing risk-weighted assets  | 1,041,540                | 872,893                  | 938,678                         |

**Capital structure**

|   | At<br>30 June<br>2007<br>US\$m | At<br>30 June<br>2006<br>US\$m | At<br>31<br>December<br>2006<br>US\$m |
|---|--------------------------------|--------------------------------|---------------------------------------|
| <b>Composition of regulatory capital</b>  |                                |                                |                                       |
| Tier 1 capital  |                                |                                |                                       |
| Shareholders' equity  | 119,780                        | 101,381                        | 108,352                               |
| Minority interests and preference shares  | 5,668                          | 6,734                          | 7,413                                 |
| Innovative tier 1 securities  | 9,874                          | 9,601                          | 9,932                                 |
| Less:   |                                |                                |                                       |
| Goodwill capitalised and intangible assets  | (37,547)                       | (33,992)                       | (36,489)                              |
| Other regulatory adjustments  | (431)                          | (1,586)                        | (1,366)                               |
| Total qualifying tier 1 capital   | 97,344                         | 82,138                         | 87,842                                |
| Tier 2 capital  |                                |                                |                                       |
| Reserves arising from revaluation of property and unrealised gains on available-for-sale equities | 3,653                          | 2,040                          | 2,982                                 |
| Collective impairment allowances  | 11,735                         | 9,087                          | 11,077                                |
| Perpetual subordinated debt   | 3,387                          | 3,665                          | 3,396                                 |
| Term subordinated debt  | 30,901                         | 27,446                         | 30,677                                |
| Minority and other interests in tier 2 capital  | 425                            | 425                            | 425                                   |
| Total qualifying tier 2 capital before deductions   | 50,101                         | 42,663                         | 48,557                                |

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|   |                  |          |          |
|---|------------------|----------|----------|
| Unconsolidated investments <sup>1</sup>                               | <b>(9,883)</b>   | (6,441)  | (7,512)  |
| Investments in capital of other banks                                 |                  | (1,419)  | (1,419)  |
| Other deductions  | <b>(520)</b>     | (305)    | (394)    |
| <b>Total regulatory capital</b>                                       | <b>137,042</b>   | 116,636  | 127,074  |
| <b>Risk-weighted assets</b>   |                  |          |          |
| Banking book  | <b>949,958</b>   | 798,577  | 857,198  |
| Trading book  | <b>91,582</b>    | 74,316   | 81,480   |
| <b>Total</b>  | <b>1,041,540</b> | 872,893  | 938,678  |
| Risk-weighted assets were included in the above totals in respect of: |                  |          |          |
| contingent liabilities  | <b>51,989</b>    | 44,761   | 44,704   |
| commitments   | <b>62,877</b>    | 55,002   | 58,569   |
| <b>Capital ratios</b>   |                  |          |          |
|   | <b>%</b>         | <b>%</b> | <b>%</b> |
| Total capital   | <b>13.2</b>      | 13.4     | 13.5     |
| Tier 1 capital  | <b>9.3</b>       | 9.4      | 9.4      |

1 Mainly comprises investments in insurance entities.

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HSBC HOLDINGS PLC

**The Management of Risk** (continued)

The above figures were computed in accordance with the FSA's requirements.

Comparisons discussed below are with the 31 December 2006 position.

Tier 1 capital increased by US\$9.5 billion. Retained profits contributed US\$4.7 billion. Shares issued, including those issued in lieu of dividends, contributed US\$2.9 billion while exchange differences added US\$2.2 billion. This was partly offset by a net decrease of US\$0.3 billion as a result of regulatory rules implemented with effect from 1 January 2007 and other regulatory adjustments.

Total risk-weighted assets increased by US\$103 billion, or 11 per cent. The proportional

consolidation of banking associates, mainly Bank of Communications and Industrial Bank, contributed US\$40 billion of this increase and a further US\$40 billion related to balance sheet growth, mainly in the loan book, net of credit risk mitigation strategies. Increased underlying trading book activity contributed US\$9 billion and the weakening US dollar gave rise to an increase of US\$14 billion.

**Risk-weighted assets by principal subsidiary**

In order to give an indication of how HSBC's capital is deployed, the table below analyses the disposition of risk-weighted assets by principal subsidiary. The risk-weighted assets are calculated using FSA rules and exclude intra-HSBC items.

|  | At<br>30 June<br>2007<br>US\$m | At<br>30 June<br>2006<br>US\$m | At<br>31<br>December<br>2006<br>US\$m |
|--|--------------------------------|--------------------------------|---------------------------------------|
| <b>Risk-weighted assets</b>  |                                |                                |                                       |
| Hang Seng Bank   | 60,263                         | 43,608                         | 43,607                                |
| The Hongkong and Shanghai Banking Corporation and other subsidiaries | 189,131                        | 131,248                        | 137,685                               |
| The Hongkong and Shanghai Banking Corporation                        | 249,394                        | 174,856                        | 181,292                               |
| HSBC Private Banking Holdings (Suisse)                               | 30,616                         | 24,876                         | 26,476                                |
| HSBC France  | 65,054                         | 59,233                         | 60,406                                |
| HSBC Bank and other subsidiaries                                     | 285,200                        | 252,263                        | 273,146                               |
| HSBC Bank  | 380,870                        | 336,372                        | 360,028                               |
| HSBC Finance   | 140,859                        | 137,284                        | 141,589                               |
| HSBC Bank Canada   | 43,617                         | 33,498                         | 35,674                                |
| HSBC Bank USA and other subsidiaries                                 | 141,772                        | 125,219                        | 140,062                               |
| HSBC North America   | 326,248                        | 296,001                        | 317,325                               |
| HSBC Mexico  | 16,770                         | 13,013                         | 15,406                                |
| HSBC Bank Middle East  | 21,097                         | 16,105                         | 17,977                                |
| HSBC Bank Malaysia   | 7,764                          | 6,555                          | 7,201                                 |
| HSBC Brazil  | 22,009                         | 16,341                         | 17,666                                |
| Grupo Banistmo   | 6,696                          |                                | 6,434                                 |

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|                         |                         |                |                |
|-------------------------|-------------------------|----------------|----------------|
| Bank of Bermuda         | <b>4,611</b>            | 4,025          | 4,370          |
| HSBC Holdings sub-group | <b>827</b>              | 455            | 876            |
| Other                   | <b>5,254</b>            | 9,170          | 10,103         |
|                         | <u><b>1,041,540</b></u> | <u>872,893</u> | <u>938,678</u> |

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HSBC HOLDINGS PLC

## Board of Directors and Senior Management

### Directors

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#### **S K Green**, Group Chairman

Age 58. An executive Director since 1998; Group Chief Executive from 2003 to May 2006. Joined HSBC in 1982. Chairman of HSBC Bank plc, HSBC North America Holdings Inc. and HSBC Private Banking Holdings (Suisse) SA. A Director of HSBC France and The Hongkong and Shanghai Banking Corporation Limited. Group Treasurer from 1992 to 1998. Executive Director, Corporate, Investment Banking and Markets from 1998 to 2003. Chairman of The British Bankers' Association.

#### \* **The Baroness Dunn**, DBE, Deputy Chairman

Age 67. An executive Director of John Swire & Sons Limited and a Director of Swire Pacific Limited. A non-executive Director since 1990 and a non-executive Deputy Chairman since 1992. A member of the Nomination Committee. A non-executive Director of The Hongkong and Shanghai Banking Corporation Limited from 1981 to 1996. A Patron of the UK Foundation of the University of British Columbia, a registered charity. A member of The Hong Kong Association and the Asia Task Force. A former Senior Member of the Hong Kong Executive Council and Legislative Council.

#### \* **Sir Brian Moffat**, OBE, Deputy Chairman

Age 68. A non-executive Director since 1998 and a non-executive Deputy Chairman since 2001. A member of the Nomination Committee. Senior independent non-executive Director until the conclusion of the Annual General Meeting on 25 May 2007. A non-executive Director of Macsteel Global BV. Former Chairman of Corus Group plc and a former member of the Court of the Bank of England.

#### **M F Geoghegan**, CBE, Group Chief Executive

Age 53. An executive Director since 2004. Joined HSBC in 1973. Chairman of HSBC Bank USA, N. A., HSBC USA Inc. and HSBC Bank Canada. Deputy Chairman of HSBC Bank plc. A Director of The Hongkong and Shanghai Banking Corporation Limited, HSBC France, HSBC North America Holdings Inc. and HSBC National Bank USA. President of HSBC Bank Brasil S.A.-Banco Múltiplo from 1997 to 2003 and responsible for all of HSBC's business throughout South America from 2000 to 2003. Chief Executive of HSBC Bank plc from 2004 to March 2006. A non-executive Director and Chairman of Young Enterprise.

#### \* **The Rt Hon the Lord Butler of Brockwell**, KG, GCB, CVO

Age 69. Master, University College, Oxford. A non-executive Director since 1998. Chairman of the Corporate Responsibility Committee and the HSBC Global Education Trust. A non-executive Director of Imperial Chemical Industries plc. A member of the International Advisory Board of Marsh McLennan Inc. Chaired the UK Government Review of Intelligence on Weapons of Mass Destruction in 2004. Secretary of the Cabinet and Head of the Home Civil Service in the United Kingdom from 1988 to 1998.

#### **J D Coombe**

Age 62. Chairman of Hogg Robinson plc. A non-executive Director since 2005. A member of the Group Audit Committee and of the Remuneration Committee. A non-executive Director of Home Retail Group plc and a member of the Supervisory Board of Siemens AG. A trustee of the Royal Academy Trust. Former executive Director and Chief Financial Officer of GlaxoSmithKline plc. A former Chairman of The Hundred Group of Finance Directors and a former member of the Accounting Standards Board.

**R A Fairhead**

Age 45. Chief Executive Officer and Director of the Financial Times Group Limited and a Director of Pearson plc. A non-executive Director since 2004. Chairman of the Group Audit Committee. A non-executive Director of The Economist Newspaper Limited. Finance Director of Pearson plc from 2002 to June 2006. Former Executive Vice President, Strategy and Group Control of Imperial Chemical Industries plc.

**D J Flint, CBE, Group Finance Director**

Age 52. Joined HSBC as an executive Director in 1995. Non-executive Chairman of HSBC Finance Corporation. A non-executive Director of BP p.l.c. and a member of the Consultative Committee of the Large Business Advisory Board of HM Revenue & Customs. Chaired the Financial Reporting Council's review of the Turnbull Guidance on Internal Control. Served on the Accounting Standards Board and the Standards Advisory Council of the International Accounting Standards Board from 2001 to 2004. A former partner in KPMG.

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HSBC HOLDINGS PLC

## Board of Directors and Senior Management (continued)

### \* **W K L Fung, OBE**

Age 58. Group Managing Director of Li & Fung Limited. A non-executive Director since 1998. A member of the Corporate Responsibility Committee. Deputy Chairman of The Hongkong and Shanghai Banking Corporation Limited. A non-executive Director of CLP Holdings Limited, Integrated Distribution Services Group Limited, Convenience Retail Asia Limited, Shui On Land Limited and VTech Holdings Limited. A member of the Hong Kong Trade Development Council. A former non-executive Director of Bank of Communications Co. Ltd. Former Chairman of the Hong Kong General Chamber of Commerce, the Hong Kong Exporters Association and the Pacific Economic Co-operation Committee.

### **J W J Hughes-Hallett**

Age 57. Chairman of John Swire & Sons Limited. A non-executive Director since 2005. A member of the Group Audit Committee and of the Nomination Committee. A non-executive Director of The Hongkong and Shanghai Banking Corporation Limited from 1999 to 2004. A non-executive Director and formerly Chairman of Cathay Pacific Airways Limited and Swire Pacific Limited. A Director of China Festival 2008. A trustee of the Dulwich Picture Gallery and the Esmée Fairbairn Foundation. A member of The Hong Kong Association and of the Governing Body of the School of Oriental and African Studies, University of London.

### **Sir Mark Moody-Stuart, KCMG**

Age 66. Chairman of Anglo American plc. A non-executive Director since 2001. Chairman of the Remuneration Committee and a member of the Corporate Responsibility Committee. A non-executive Director of Accenture Limited, a Governor of Nuffield Hospitals and President of the Liverpool School of Tropical Medicine. Chairman of the Global Business Coalition on HIV/AIDS and the Global Compact Foundation. A former Director and Chairman of The Shell Transport and Trading Company, plc and former Chairman of the Committee of Managing Directors of the Royal Dutch/Shell Group of Companies.

### **G Morgan**

Age 61. A non-executive Director since October 2006. A member of the Remuneration Committee. Non-executive Chairman of SNC-Lavalin Group Inc. A member of the Board of Trustees of The Fraser Institute and the Energy Advisory Board of Accenture Limited. A non-executive Director of HSBC Bank Canada from 1996 to April 2006. Founding President and Chief Executive Officer of EnCana Corporation until December 2005 and Vice Chairman from December 2005 to October 2006. A former Director of Alcan Inc.

### **S W Newton**

Age 65. Chairman of The Real Return Group Limited. A non-executive Director since 2002. A member of the Group Audit Committee. A Member of the Advisory Board of the East Asia Institute and of the Investment Board at Cambridge

University. A Member of The Wellcome Trust Investment Committee. Founder of Newton Investment Management, from which he retired in 2002.

**S M Robertson**, Senior Independent Non- Executive Director

Age 66. Non-executive Chairman of Rolls-Royce Group plc and the founder member of Simon Robertson Associates LLP. A non-executive Director since January 2006 and senior independent non-executive Director since 25 May 2007. A Member of the Nomination Committee. A non- executive Director of Berry Bros. & Rudd Limited, The Economist Newspaper Limited and The Royal Opera House Covent Garden Limited. Chairman of Trustees of the Ernest Kleinwort Charitable Trust. A trustee of the Eden Project and of the Royal Opera House Endowment Fund. A former Managing Director of Goldman Sachs International. Former Chairman of Dresdner Kleinwort Benson and a former non-executive Director of Inchcape plc, Invensys plc and the London Stock Exchange plc.

**Sir Brian Williamson**, CBE

Age 62. Chairman of Electra Private Equity plc. A non-executive Director since 2002. Chairman of the Nomination Committee. A non-executive Director of NYSE Euronext and a Director of Resolution plc. A senior adviser to Fleming Family and Partners. Former Chairman of London International Financial Futures and Options Exchange, Gerrard Group plc and Resolution Life Group Limited. A former non- executive Director of the Financial Services Authority and of the Court of The Bank of Ireland.

\* *Non-executive Director  
Independent non-executive  
Director*

## **Adviser to the Board**

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### **D J Shaw**

Age 61. An Adviser to the Board since 1998. Solicitor. A partner in Norton Rose from 1973 to 1998. A Director of The Bank of Bermuda Limited

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and HSBC Private Banking Holdings (Suisse) SA. A non-executive Director of Kowloon Development Company Limited and Shui On Land Limited.

## Secretary

---

### **R G Barber**

Age 56. Group Company Secretary. A Group General Manager since October 2006. Joined HSBC in 1980. Company Secretary of HSBC Holdings plc since 1990. Corporation Secretary of The Hongkong and Shanghai Banking Corporation Limited from 1986 to 1992 and Company Secretary of HSBC Bank plc from 1994 to 1996.

## Group Managing Directors

---

### **C C R Bannister**

Age 48. Group Managing Director, Insurance. A Group Managing Director since August 2006. Joined HSBC in 1994. Appointed a Group General Manager in 2001. Chairman of HSBC Insurance Holdings Limited. Deputy Chief Executive Officer, HSBC Securities (USA) Inc. from 1996 to 1998 and Chief Executive Officer, Group Private Banking from 1998 to 2006.

### **V H C Cheng, OBE**

Age 59. Chairman of The Hongkong and Shanghai Banking Corporation Limited. A Group Managing Director since 2005. Joined HSBC in 1978. Appointed a Group General Manager in 1995. Deputy Chairman and Chief Executive Officer of Hang Seng Bank Limited from 1998 to 2005.

### **C-H Filippi**

Age 54. Chairman and Chief Executive Officer of HSBC France until he retires on 1 September 2007, following which he will continue as non-executive Chairman of HSBC France. A Group Managing Director since 2004. A Director of HSBC Bank plc and a member of the Supervisory Board of HSBC Trinkaus & Burkhardt AG. Joined HSBC France in 1987 having previously held senior appointments in the French civil service. Appointed a Group General Manager in 2001. Global Head of Corporate and Institutional Banking from 2001 to 2004.

### **A A Flockhart**

Age 55. Chief Executive Officer of The Hongkong and Shanghai Banking Corporation Limited since 25 July 2007. Global Head of Commercial Banking since 9 July 2007. A Group Managing Director since October 2006. Joined HSBC in 1974. Appointed a Group General Manager in 2002. Managing Director of The Saudi British Bank from 1997 to 1999 and Senior Executive Vice-President, Commercial Banking, HSBC Bank USA, N.A. from 1999 to 2002. Chief Executive Officer, Mexico from 2002 to October 2006. President and Group Managing Director Latin America and the Caribbean from October 2006 to 20 July 2007.

### **S T Gulliver**

Age 48. Head of Corporate, Investment Banking and Markets and Group Investment Businesses. A Group Managing Director since 2004. A Director of HSBC Bank plc, HSBC USA Inc. and The Hongkong and Shanghai Banking Corporation Limited. A member of the Supervisory

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Board of HSBC Trinkaus & Burkhardt AG. Joined HSBC in 1980. Appointed a Group General Manager in 2000. Head of Treasury and Capital Markets in Asia-Pacific from 1996 to 2002, Head of Global Markets from 2002 to 2003 and Co-Head of Corporate, Investment Banking and Markets from 2003 to May 2006.

### **D H Hodgkinson**

Age 56. Group Chief Operating Officer. A Group Managing Director since May 2006. Chairman of HSBC Bank Middle East Limited. Joined HSBC in 1969. Appointed a Group General Manager in 2003. Managing Director of The Saudi British Bank from 1999 to 2003. Deputy Chairman and Chief Executive Officer of HSBC Bank Middle East Limited from 2003 to May 2006.

### **D D J John**

Age 57. Director and Chief Executive, HSBC Bank plc. A Group Managing Director since March 2006. Joined HSBC Bank plc in 1971. Appointed a Group General Manager in 2000. Deputy Chairman and Chief Executive Officer, HSBC Bank Malaysia Bhd from 1999 to 2002. Chief Operating Officer of HSBC Bank plc from 2003 to May 2005 and Deputy Chief Executive from May 2005 to March 2006.

### **Y A Nasr**

Age 52. Group Managing Director, Strategic Investments since October 2006 and Chief Executive Officer of HSBC Bank Middle East Limited since 22 May 2007. A Director of HSBC Private Banking Holdings (Suisse) SA. A Group Managing Director since 2004. Joined HSBC in 1976. Appointed a Group General Manager in 1998. President and Chief Executive Officer of HSBC Bank Canada from 1997 to 1999. President and Chief Executive Officer of HSBC USA Inc. and HSBC Bank USA from 1999 to 2003. President, HSBC Bank Brasil S.A.-Banco Múltiplo from 2003 to 2006.

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HSBC HOLDINGS PLC

**Financial Statements (unaudited)****Consolidated income statement for the half-year to 30 June 2007**

|   | Half-year to                      |                          |                                 |
|---|-----------------------------------|--------------------------|---------------------------------|
|   | <b>30 June<br/>2007<br/>US\$m</b> | 30 June<br>2006<br>US\$m | 31<br>December<br>2006<br>US\$m |
|   | <i>Notes</i>                      |                          |                                 |
| Interest income   | 43,567                            | 35,785                   | 40,094                          |
| Interest expense  | (25,337)                          | (19,054)                 | (22,339)                        |
| Net interest income   | 18,230                            | 16,731                   | 17,755                          |
| Fee income  | 12,488                            | 10,441                   | 10,639                          |
| Fee expense   | (1,993)                           | (2,061)                  | (1,837)                         |
| Net fee income  | 10,495                            | 8,380                    | 8,802                           |
| Trading income excluding net interest income  | 3,351                             | 3,112                    | 2,507                           |
| Net interest income on trading activities   | 2,160                             | 1,149                    | 1,454                           |
| Net trading income  | 5,511                             | 4,261                    | 3,961                           |
| Net income from financial instruments designated at fair value                              | 874                               | 260                      | 397                             |
| Gains less losses from financial investments  | 999                               | 493                      | 476                             |
| Gains arising from dilution of interests in associates                                      | 19                                | 1,076                    |                                 |
| Dividend income   | 252                               | 222                      | 118                             |
| Net earned insurance premiums   | 3,977                             | 2,834                    | 2,834                           |
| Other operating income  | 678                               | 1,153                    | 1,393                           |
| <b>Total operating income</b>   | <b>42,092</b>                     | <b>34,334</b>            | <b>35,736</b>                   |
| Net insurance claims incurred and movement in policyholders' liabilities                    | (3,599)                           | (2,149)                  | (2,555)                         |
| <b>Net operating income before loan impairment charges and other credit risk provisions</b> | <b>38,493</b>                     | <b>32,185</b>            | <b>33,181</b>                   |
| Loan impairment charges and other credit risk provisions                                    | (6,346)                           | (3,890)                  | (6,683)                         |
| <b>Net operating income</b>   | <b>32,147</b>                     | <b>28,295</b>            | <b>26,498</b>                   |
| Employee compensation and benefits  | (10,430)                          | (8,992)                  | (9,508)                         |
| General and administrative expenses   | (7,022)                           | (6,065)                  | (6,758)                         |
| Depreciation and impairment of property, plant and equipment                                | (817)                             | (748)                    | (766)                           |
| Amortisation and impairment of intangible assets  | (342)                             | (334)                    | (382)                           |
| <b>Total operating expenses</b>   | <b>(18,611)</b>                   | <b>(16,139)</b>          | <b>(17,414)</b>                 |
| <b>Operating profit</b>   | <b>13,536</b>                     | <b>12,156</b>            | <b>9,084</b>                    |



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|   |    |                |                |                |
|---|----|----------------|----------------|----------------|
| Share of profit in associates and joint ventures          |    | <u>623</u>     | <u>361</u>     | <u>485</u>     |
| <b>Profit before tax</b>                                  |    | <b>14,159</b>  | 12,517         | 9,569          |
| Tax expense   | 6  | <u>(2,645)</u> | <u>(3,272)</u> | <u>(1,943)</u> |
| <b>Profit for the period</b>                              |    | <b>11,514</b>  | 9,245          | 7,626          |
| Profit attributable to shareholders of the parent company | 15 | <b>10,895</b>  | 8,729          | 7,060          |
| Profit attributable to minority interests                 | 15 | <b>619</b>     | 516            | 566            |
|   |    | <b>US\$</b>    | US\$           | US\$           |
| Basic earnings per ordinary share                         | 4  | <b>0.95</b>    | 0.78           | 0.62           |
| Diluted earnings per ordinary share                       | 4  | <b>0.94</b>    | 0.77           | 0.62           |
| Dividends per ordinary share                              | 3  | <b>0.53</b>    | 0.46           | 0.30           |

[Back to Contents](#)**Consolidated balance sheet at 30 June 2007**

|  |              | At<br>30 June<br>2007<br>US\$m | At<br>30 June<br>2006<br>US\$m | At<br>31<br>December<br>2006<br>US\$m |
|--|--------------|--------------------------------|--------------------------------|---------------------------------------|
|  | <i>Notes</i> |                                |                                |                                       |
| <b>ASSETS</b>                                      |              |                                |                                |                                       |
| Cash and balances at central banks                 |              | 16,651                         | 24,343                         | 12,732                                |
| Items in the course of collection from other banks |              | 23,152                         | 12,425                         | 14,144                                |
| Hong Kong Government certificates of indebtedness  |              | 12,947                         | 12,588                         | 13,165                                |
| Trading assets                                     | 7            | 424,645                        | 299,295                        | 328,147                               |
| Financial assets designated at fair value          | 8            | 34,849                         | 16,855                         | 20,573                                |
| Derivatives  | 9            | 149,181                        | 104,665                        | 103,702                               |
| Loans and advances to banks                        |              | 214,645                        | 162,482                        | 185,205                               |
| Loans and advances to customers                    |              | 928,101                        | 814,209                        | 868,133                               |
| Financial investments                              | 10           | 233,001                        | 192,334                        | 204,806                               |
| Interests in associates and joint ventures         |              | 8,583                          | 7,795                          | 8,396                                 |
| Goodwill and intangible assets                     |              | 38,445                         | 34,544                         | 37,335                                |
| Property, plant and equipment                      |              | 14,982                         | 15,277                         | 16,424                                |
| Other assets                                       | 11           | 34,166                         | 27,542                         | 33,444                                |
| Prepayments and accrued income                     |              | 17,093                         | 13,784                         | 14,552                                |
|  |              | <hr/>                          | <hr/>                          | <hr/>                                 |
| Total assets                                       |              | 2,150,441                      | 1,738,138                      | 1,860,758                             |
|  |              | <hr/>                          | <hr/>                          | <hr/>                                 |
| <b>LIABILITIES AND EQUITY</b>                      |              |                                |                                |                                       |
| <b>Liabilities</b>                                 |              |                                |                                |                                       |
| Hong Kong currency notes in circulation            |              | 12,947                         | 12,588                         | 13,165                                |
| Deposits by banks                                  |              | 128,773                        | 83,139                         | 99,694                                |
| Customer accounts                                  |              | 980,832                        | 833,742                        | 896,834                               |
| Items in the course of transmission to other banks |              | 20,339                         | 9,532                          | 12,625                                |
| Trading liabilities                                | 12           | 313,193                        | 228,116                        | 226,608                               |
| Financial liabilities designated at fair value     | 13           | 75,966                         | 64,354                         | 70,211                                |
| Derivatives  | 9            | 144,284                        | 103,660                        | 101,478                               |
| Debt securities in issue                           |              | 229,239                        | 209,309                        | 230,325                               |
| Retirement benefit liabilities                     |              | 2,984                          | 3,722                          | 5,555                                 |
| Other liabilities                                  |              | 34,500                         | 31,669                         | 29,824                                |
| Liabilities under insurance contracts              |              | 36,929                         | 15,663                         | 17,670                                |
| Accruals and deferred income                       |              | 16,857                         | 12,584                         | 16,310                                |
| Provisions   |              | 3,603                          | 2,286                          | 2,859                                 |
| Subordinated liabilities                           |              | 23,504                         | 20,404                         | 22,672                                |
|  |              | <hr/>                          | <hr/>                          | <hr/>                                 |
| Total liabilities                                  |              | 2,023,950                      | 1,630,768                      | 1,745,830                             |
|  |              | <hr/>                          | <hr/>                          | <hr/>                                 |
| <b>Equity</b>                                      |              |                                |                                |                                       |
| Called up share capital                            |              | 5,857                          | 5,741                          | 5,786                                 |
| Share premium account                              |              | 7,834                          | 7,236                          | 7,789                                 |

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|                              |                          |                   |                   |
|------------------------------|--------------------------|-------------------|-------------------|
| Other reserves               | <b>31,838</b>            | 26,394            | 29,380            |
| Retained earnings            | <b>74,251</b>            | 62,010            | 65,397            |
|                              | <u>          </u>        | <u>          </u> | <u>          </u> |
| Total shareholders' equity   | <b>119,780</b>           | 101,381           | 108,352           |
| Minority interests           | <b>6,711</b>             | 5,989             | 6,576             |
|                              | <u>          </u>        | <u>          </u> | <u>          </u> |
| Total equity                 | <i>15</i> <b>126,491</b> | 107,370           | 114,928           |
|                              | <u>          </u>        | <u>          </u> | <u>          </u> |
| Total equity and liabilities | <b>2,150,441</b>         | 1,738,138         | 1,860,758         |
|                              | <u>          </u>        | <u>          </u> | <u>          </u> |

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**Financial Statements (unaudited)** (continued)**Consolidated statement of recognised income and expense for the half-year to 30 June 2007**

|  | Half-year to   |         |          |
|--|----------------|---------|----------|
|  | <b>30 June</b> | 30 June | 31       |
|  | <b>2007</b>    | 2006    | December |
|  | <b>US\$m</b>   | US\$m   | US\$m    |
| Available-for-sale investments:  |                |         |          |
| fair value gains/(losses) taken to equity                                | <b>1,162</b>   | (476)   | 2,058    |
| fair value gains transferred to income statement on disposabl impairment | <b>(783)</b>   | (319)   | (325)    |
| Cash flow hedges:  |                |         |          |
| fair value gains taken to equity   | <b>395</b>     | 147     | 1,407    |
| fair value gains transferred to income statement                         | <b>(568)</b>   | (177)   | (2,021)  |
| Share of changes in equity of associates and joint ventures              | <b>186</b>     | (44)    | 64       |
| Exchange differences   | <b>2,293</b>   | 3,203   | 1,472    |
| Actuarial gains/(losses) on defined benefit schemes                      | <b>2,028</b>   | 1,477   | (1,555)  |
|  | <b>4,713</b>   | 3,811   | 1,100    |
| Tax on items taken directly to equity                                    | <b>(455)</b>   | (196)   | 152      |
| Total income and expense taken to equity during the period               | <b>4,258</b>   | 3,615   | 1,252    |
| Profit for the period  | <b>11,514</b>  | 9,245   | 7,626    |
| Total recognised income and expense for the period                       | <b>15,772</b>  | 12,860  | 8,878    |
| Total recognised income and expense for the period attributable to:      |                |         |          |
| shareholders of the parent company                                       | <b>14,950</b>  | 12,292  | 8,235    |
| minority interests   | <b>822</b>     | 568     | 643      |
|  | <b>15,772</b>  | 12,860  | 8,878    |

[Back to Contents](#)**Consolidated cash flow statement for the half-year to 30 June 2007**

|  | <i>Notes</i> | Half-year to     |           |             |
|--|--------------|------------------|-----------|-------------|
|  |              | <b>30 June</b>   | 30 June   | 31 December |
|  |              | <b>2007</b>      | 2006      | 2006        |
|  |              | US\$m            | US\$m     | US\$m       |
| <b>Cash flows from operating activities</b>                                |              |                  |           |             |
| Profit before tax  |              | <b>14,159</b>    | 12,517    | 9,569       |
| Adjustments for:   |              |                  |           |             |
| non-cash items included in profit before tax                               | 16           | <b>8,434</b>     | 5,681     | 9,275       |
| change in operating assets   | 16           | <b>(65,685)</b>  | (106,213) | (67,056)    |
| change in operating liabilities  | 16           | <b>123,248</b>   | 136,184   | 101,194     |
| elimination of exchange differences <sup>1</sup>                           |              | <b>(5,871)</b>   | (8,203)   | (3,911)     |
| net gain from investing activities   |              | <b>(2,225)</b>   | (752)     | (1,262)     |
| share of profit in associates and joint ventures                           |              | <b>(623)</b>     | (361)     | (485)       |
| dividends received from associates   |              | <b>146</b>       | 32        | 65          |
| contribution paid to post-employment defined benefit plans                 |              | <b>(970)</b>     | (236)     | (311)       |
| tax paid   |              | <b>(2,217)</b>   | (1,983)   | (2,963)     |
| Net cash from operating activities   |              | <b>68,396</b>    | 36,666    | 44,115      |
| <b>Cash flows from investing activities</b>                                |              |                  |           |             |
| Purchase of financial investments  |              | <b>(248,734)</b> | (181,454) | (104,862)   |
| Proceeds from the sale of financial investments                            |              | <b>237,481</b>   | 177,762   | 96,012      |
| Purchase of property, plant and equipment                                  |              | <b>(965)</b>     | (803)     | (1,597)     |
| Proceeds from the sale of property, plant and equipment                    |              | <b>1,368</b>     | 915       | 1,589       |
| Purchase of intangible assets  |              | <b>(451)</b>     | (352)     | (500)       |
| Net cash outflow from acquisition of and increase in stake of subsidiaries |              | <b>(323)</b>     | (5)       | (1,180)     |
| Net cash inflow from disposal of subsidiaries                              |              |                  | 23        | 39          |
| Net cash outflow from acquisition of and increase in stake of associates   |              | <b>(9)</b>       | (208)     | (377)       |
| Proceeds from disposal of associates                                       |              |                  | 319       | 555         |
| Net cash used in investing activities                                      |              | <b>(11,633)</b>  | (3,803)   | (10,321)    |
| <b>Cash flows from financing activities</b>                                |              |                  |           |             |
| Issue of ordinary share capital  |              | <b>116</b>       | 414       | 596         |
| Issue of preference shares   |              |                  | 374       |             |
| Net purchases and sales of own shares for market-making purposes           |              | <b>220</b>       | (141)     | 187         |
| Purchases of own shares to meet share awards and share option awards       |              | <b>(807)</b>     | (526)     | (49)        |
| On exercise of share options   |              | <b>58</b>        | 137       | 36          |
| Subordinated loan capital issued   |              | <b>563</b>       | 3,716     | 2,232       |
| Subordinated loan capital repaid   |              | <b>(87)</b>      | (273)     | (630)       |
| Dividends paid to shareholders of the parent company                       |              | <b>(3,591)</b>   | (3,202)   | (2,725)     |
| Dividends paid to minority interests                                       |              | <b>(460)</b>     | (533)     | (177)       |
| Net cash used in financing activities                                      |              | <b>(3,988)</b>   | (34)      | (530)       |

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|  |                   |                   |                   |
|--|-------------------|-------------------|-------------------|
| <b>Net increase in cash and cash equivalents</b>             | <b>52,775</b>     | 32,829            | 33,264            |
| Cash and cash equivalents at the beginning of the period     | <b>215,486</b>    | 141,307           | 178,626           |
| Exchange differences in respect of cash and cash equivalents | <b>4,023</b>      | 4,490             | 3,596             |
|  | <u>          </u> | <u>          </u> | <u>          </u> |
| <b>Cash and cash equivalents at the end of the period</b>    | <b>16 272,284</b> | 178,626           | 215,486           |
|  | <u>          </u> | <u>          </u> | <u>          </u> |

1 *Adjustment to bring changes between opening and closing balance sheet amounts to average rates. This is not done on a line-by-line basis, as details cannot be determined without unreasonable expense.*

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**Notes on the Financial Statements (unaudited)**

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**1 Basis of preparation****(a) Compliance with International Financial Reporting Standards**

These interim consolidated financial statements have been prepared in accordance with IAS 34 *Interim Financial Reporting* .

HSBC has prepared its consolidated financial statements in accordance with IFRSs as endorsed by the EU. EU- endorsed IFRSs may differ temporarily from IFRSs, as published by the IASB, if a new or amended IFRS has not been endorsed by the EU by the period end. There were no unendorsed standards affecting this interim statement. As at 30 June 2007, there is no difference between IFRSs as endorsed by the EU and IFRSs as issued by the IASB in terms of their application to HSBC.

IFRSs comprise accounting standards issued by the IASB and its predecessor body as well as interpretations issued by the International Financial Reporting Interpretations Committee ( IFRIC ) and its predecessor body.

The primary financial statements in this document are presented in accordance with IAS 1 *Presentation of Financial Statements* .

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On 1 January 2007, HSBC adopted IFRIC 10 Interim Financial Reporting and Impairment and IFRIC 11 Group and Treasury Share Transactions . The application of these interpretations had no significant effect on the consolidated financial statements.

HSBC also provides details of its net income and shareholders' equity calculated in accordance with US GAAP. US GAAP differs in certain respects from IFRSs. Details of these differences in respect of this interim period will be published in September 2007.

### (b) Consolidation

The interim consolidated financial statements of HSBC comprise the financial statements of HSBC Holdings and its subsidiaries.

The method adopted by HSBC to consolidate its subsidiaries is described on page 302 of the *Annual Report and Accounts 2006*.

### (c) Use of estimates and assumptions

When preparing the financial statements, it is the Directors' responsibility under UK company law to select suitable accounting policies and to make judgements and estimates that are reasonable and prudent. The preparation of financial information requires the use of estimates and assumptions about future conditions. Use of available information and application of judgement are inherent in the formation of estimates. Actual results in the future may differ from those reported. In this regard, management believes that the critical accounting



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policies where judgement is necessarily applied are those which relate to loan impairment, goodwill impairment and the valuation of financial instruments. These critical accounting policies are described in pages 111 to 115 of the *Annual Report and Accounts 2006*.

## (d) Future accounting developments.

There are currently no IFRSs or Interpretations that have been issued by the IASB and endorsed by the EU which become effective after 30 June 2007 that have not been adopted by HSBC.

**Standards and Interpretations issued by the IASB but not endorsed by the EU**

IFRS 8 Operating Segments ( IFRS 8 ), which replaces IAS 14 Segment Reporting ( IAS 14 ), was issued on 30 November 2006 and is effective for annual periods beginning on or after 1 January 2009. This standard specifies how an entity should report information about its operating segments, based on information about the components of the entity that management uses to make operating decisions. HSBC currently presents two sets of segments in accordance with IAS 14, one geographical and one based on customer groups, which reflect the way the businesses of the Group are managed. HSBC currently expects to adopt IFRS 8 with effect from 1 January 2009, and will accordingly present segmental information which reflects the operating segments used to make operating decisions at that time.

The IASB issued a revised IAS 23 Borrowing Costs on 29 March 2007, which is applicable for annual periods beginning on or after 1 January 2009. The revised Standard eliminates the option of recognising borrowing costs immediately as an expense, to the extent that they are directly attributable to the acquisition, construction or production of a qualifying asset. HSBC does not expect adoption of the revised Standard to have a significant impact on Group results.

IFRIC 12 Service Concession Arrangements ( IFRIC 12 ) was issued on 30 November 2006 and is effective for annual periods beginning on or after 1 January 2008. IFRIC 12 provides guidance on service concession arrangements by which a government or other public sector entity grants contracts for the supply of public services to private sector operators. IFRIC 12 addresses how service concession operators should apply existing IFRSs to account for the obligations they undertake and the rights they receive in service concession arrangements. IFRIC 12 is unlikely to have a material effect on the consolidated financial statements.

IFRIC 13 Customer Loyalty Programmes ( IFRIC 13 ) was issued on 28 June 2007 and is effective for annual periods beginning on or after 1 July 2008. IFRIC 13 addresses how companies that grant their customers loyalty award credits (often called points) when buying goods or services should account for their obligation to provide free or discounted goods or services if and when the customers redeem the points. IFRIC 13 requires companies to allocate some of the proceeds of the initial sale to the award credits and recognise these proceeds as revenue only when they have fulfilled their obligations to provide the goods or services. HSBC is currently assessing the effect of this interpretation on the consolidated financial statements.

IFRIC 14 IAS 19 The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction ( IFRIC 14 ) was issued on 5 July 2007 and is effective for annual periods beginning on or after 1 January 2008. IFRIC 14 provides guidance regarding the circumstances under which refunds and future reductions in contributions from a defined benefit plan can be regarded as available to an entity for the purpose of recognising a net defined benefit asset. Additionally, in jurisdictions where there is both a minimum funding requirement and restrictions over the amounts that companies can recover from the plan, either as refunds or reductions in contribution, additional liabilities may need to be recognised. IFRIC 14 is unlikely to have a material effect on the consolidated financial statements.

In the opinion of management, all normal and recurring adjustments considered necessary for a fair presentation of HSBC's net income, financial position and cash flows for interim periods have been made.

**2 Accounting policies**

The accounting policies adopted by HSBC for these interim consolidated financial statements are consistent with those described on page 304 of the *Annual Report and Accounts 2006*.

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**Notes on the Financial Statements (unaudited)** (continued)**3 Dividends**

Dividends to shareholders of the parent company were as follows:

|  | Half-year to      |                |                              |                   |                |                              |                   |                |                              |
|--|-------------------|----------------|------------------------------|-------------------|----------------|------------------------------|-------------------|----------------|------------------------------|
|  | 30 June 2007      |                |                              | 30 June 2006      |                |                              | 31 December 2006  |                |                              |
|  | Per share<br>US\$ | Total<br>US\$m | Settled<br>in scrip<br>US\$m | Per share<br>US\$ | Total<br>US\$m | Settled<br>in scrip<br>US\$m | Per share<br>US\$ | Total<br>US\$m | Settled<br>in scrip<br>US\$m |
| <b>Dividends declared on ordinary shares</b>           |                   |                |                              |                   |                |                              |                   |                |                              |
| Fourth interim dividend in respect of previous year    | 0.360             | 4,161          | 2,116                        | 0.310             | 3,513          | 1,542                        |                   |                |                              |
| First interim dividend in respect of current year      | 0.170             | 1,986          | 712                          | 0.150             | 1,712          | 248                          |                   |                |                              |
| Second interim dividend in respect of current year     |                   |                |                              |                   |                |                              | 0.150             | 1,724          | 515                          |
| Third interim dividend in respect of current year      |                   |                |                              |                   |                |                              | 0.150             | 1,730          | 223                          |
|  | <b>0.530</b>      | <b>6,147</b>   | <b>2,828</b>                 | <b>0.460</b>      | <b>5,225</b>   | <b>1,790</b>                 | <b>0.300</b>      | <b>3,454</b>   | <b>738</b>                   |
| <b>Quarterly dividends on preference share capital</b> |                   |                |                              |                   |                |                              |                   |                |                              |
| March dividend   | 15.50             | 22             |                              | 15.50             | 22             |                              |                   |                |                              |
| June dividend  | 15.50             | 23             |                              | 15.50             | 23             |                              |                   |                |                              |
| September dividend                                     |                   |                |                              |                   |                |                              | 15.50             | 22             |                              |
| December dividend                                      |                   |                |                              |                   |                |                              | 15.50             | 23             |                              |
|  | <b>31.00</b>      | <b>45</b>      |                              | <b>31.00</b>      | <b>45</b>      |                              | <b>31.00</b>      | <b>45</b>      |                              |

The Directors have declared a second interim dividend in respect of the financial year ending 31 December 2007 of US\$0.17 per ordinary share, a distribution of approximately US\$1,991 million. The second interim dividend will be payable on 4 October 2007 to holders of ordinary shares on the Register at the close of business on 17 August 2007. Further details are contained in paragraph 5 of the Additional Information section on page 166.

**4 Earnings per share**

|  | Half-year to                      |                         |                             |
|--|-----------------------------------|-------------------------|-----------------------------|
|  | 30 June<br>2007<br>US\$           | 30 June<br>2006<br>US\$ | 31 December<br>2006<br>US\$ |
|  | Basic earnings per ordinary share | 0.95                    | 0.78                        |

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Diluted earnings per ordinary share **0.94** 0.77 0.62

Basic earnings per ordinary share was calculated by dividing the earnings attributable to ordinary shareholders of the parent company US\$10,850 million by the weighted average number of ordinary shares outstanding, excluding own shares held, of 11,463 million (first half of 2006: earnings of US\$8,684 million and 11,148 million shares; second half of 2006: earnings of US\$7,015 million and 11,272 million shares).

|  | <b>30 June<br/>2007<br/>US\$m</b> | 30 June<br>2006<br>US\$m | 31 December<br>2006<br>US\$m |
|--|-----------------------------------|--------------------------|------------------------------|
| Profit attributable to shareholders of the parent company  | <b>10,895</b>                     | 8,729                    | 7,060                        |
| Dividend payable on preference shares classified as equity | <b>(45)</b>                       | (45)                     | (45)                         |
|  | <b>10,850</b>                     | 8,684                    | 7,015                        |

Diluted earnings per ordinary share was calculated by dividing the basic earnings by the weighted average number of ordinary shares outstanding, excluding own shares held, plus the weighted average number of ordinary shares that would be issued on ordinary conversion of all the dilutive potential ordinary shares, of 11,518 million (first half of 2006: 11,304 million shares; second half of 2006: 11,336 million shares).

[Back to Contents](#)**5 Post-employment benefits**

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

|                                 | Half-year to                      |                          |                              |
|---------------------------------|-----------------------------------|--------------------------|------------------------------|
|                                 | <b>30 June<br/>2007<br/>US\$m</b> | 30 June<br>2006<br>US\$m | 31 December<br>2006<br>US\$m |
| Current service cost            | <b>403</b>                        | 366                      | 413                          |
| Interest cost                   | <b>843</b>                        | 709                      | 776                          |
| Expected return on plan assets  | <b>(840)</b>                      | (769)                    | (832)                        |
| Past service cost               | <b>1</b>                          | (1)                      | 11                           |
| Curtailments                    | <b>(65)</b>                       | (3)                      | (5)                          |
| Settlements                     |                                   |                          | (1)                          |
| <b>Net defined benefit cost</b> | <b>342</b>                        | 302                      | 362                          |

HSBC revalues its defined benefit post-employment plans each year at 31 December, in consultation with the plans' local actuaries. The assumptions underlying the calculations are used to determine the expected income statement charge for the year going forward.

At 30 June each year HSBC revalues all plan assets to current market prices. HSBC also reviews the assumptions used to calculate the defined benefit obligations (the liabilities of the plans) and updates the carrying amount of the obligations if there have been significant changes as a consequence of changes in assumptions.

Rises in the average yields of high quality (AA rated or equivalent) debt instruments in certain countries in 2007, together with a rise in inflation above expectations in certain countries, have resulted in significant changes in the valuation of the defined benefit obligations. HSBC has, therefore, revalued certain plan obligations where the impact has been significant. This resulted in a net decrease in the defined benefit obligation for the HSBC Bank (UK) Pension Scheme of US\$2,232 million and for other plans of US\$467 million. All differences from expected changes were recognised directly in equity as actuarial gains.

In March 2007 HSBC made an additional contribution of US\$587 million to the HSBC Bank (UK) Pension Scheme in accordance with the schedule of additional contributions agreed by the Trustees with HSBC.

The US\$65 million curtailment gain reported in the table above results primarily from the closure of a defined benefit scheme and its replacement by a new scheme to which HSBC contributes primarily fixed payments.

The discount rates used to calculate HSBC's obligations under its defined benefit post-employment plans were as follows:

|           | <b>At<br/>30 June<br/>2007<br/>%</b> | At<br>30 June<br>2006<br>% | At<br>31 December<br>2006<br>% |
|-----------|--------------------------------------|----------------------------|--------------------------------|
| UK        | <b>5.80</b>                          | 5.25                       | 5.10                           |
| Hong Kong | <b>4.78</b>                          | 4.20                       | 3.75                           |
| US        | <b>6.30</b>                          | 6.35                       | 5.90                           |
| Jersey    | <b>5.80</b>                          | 4.75                       | 5.10                           |
| Mexico    | <b>8.00</b>                          | 8.90                       | 8.00                           |
| Brazil    | <b>10.75</b>                         | 11.75                      | 10.75                          |
| France    | <b>5.00</b>                          | 4.50                       | 4.50                           |
| Canada    | <b>5.50</b>                          | 5.25                       | 5.19                           |

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|             |             |      |      |
|-------------|-------------|------|------|
| Switzerland | <b>3.00</b> | 2.25 | 2.25 |
| Germany     | <b>5.10</b> | 4.50 | 4.50 |

The inflation rate used to calculate the HSBC Bank (UK) Pension Scheme obligation at 30 June 2007 was 3.2 per cent (30 June 2006: 2.8 per cent; 31 December 2006: 3.0 per cent). Rates of pay increase were adjusted in line with this inflation assumption. There were no changes to other assumptions.

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**Notes on the Financial Statements (unaudited)** (continued)**6 Tax expense**

|   | Half-year to             |                          |                              |
|---|--------------------------|--------------------------|------------------------------|
|   | 30 June<br>2007<br>US\$m | 30 June<br>2006<br>US\$m | 31 December<br>2006<br>US\$m |
| <b>Current tax</b>                                |                          |                          |                              |
| United Kingdom corporation tax charge             | 476                      | 536                      | 114                          |
| Overseas tax                                      | 1,937                    | 2,254                    | 2,298                        |
|   | <b>2,413</b>             | <b>2,790</b>             | <b>2,412</b>                 |
| <b>Deferred tax</b>                               |                          |                          |                              |
| Origination and reversal of temporary differences | 232                      | 482                      | (469)                        |
| Tax expense                                       | <b>2,645</b>             | <b>3,272</b>             | <b>1,943</b>                 |
| Effective tax rate (per cent)                     | <b>18.7</b>              | 26.1                     | 20.3                         |

The UK corporation tax rate applying to HSBC was 30 per cent (2006: 30 per cent). Overseas tax included Hong Kong profits tax of US\$495 million (first half of 2006: US\$387 million; second half of 2006: US\$364 million). Subsidiaries in Hong Kong provided for Hong Kong profits tax at the rate of 17.5 per cent (2006: 17.5 per cent) on the profits for the period assessable in Hong Kong. Other overseas subsidiaries and overseas branches provided for taxation at the appropriate rates in the countries in which they operate.

The following table reconciles the overall tax expense which would apply if all profits had been taxed at the UK corporation tax rate:

|   | Half-year to |             |              |             |                  |             |
|---|--------------|-------------|--------------|-------------|------------------|-------------|
|   | 30 June 2007 |             | 30 June 2006 |             | 31 December 2006 |             |
|   | US\$m        | %           | US\$m        | %           | US\$m            | %           |
| <b>Analysis of overall tax expense</b>  |              |             |              |             |                  |             |
| Taxation at UK corporation tax rate of 30 per cent (2006: 30 per cent)        | 4,248        | 30.0        | 3,756        | 30.0        | 2,870            | 30.0        |
| Effect of taxing overseas profits in principal locations at different rates   | (459)        | (3.2)       | (187)        | (1.5)       | (381)            | (4.0)       |
| Tax-free gains  | (157)        | (1.1)       | (97)         | (0.8)       | (102)            | (1.0)       |
| Adjustments in respect of prior period liabilities                            | (152)        | (1.1)       | 36           | 0.3         | (142)            | (1.5)       |
| Low income housing tax credits <sup>1</sup>                                   | (52)         | (0.4)       | (55)         | (0.4)       | (53)             | (0.6)       |
| Effect of profit in associates and joint ventures                             | (185)        | (1.3)       | (100)        | (0.8)       | (153)            | (1.6)       |
| Effect of previously unrecognised temporary differences <sup>2</sup>          | (211)        | (1.5)       | (45)         | (0.4)       | (77)             | (0.8)       |
| Impact of gains arising from dilution of interests in associates <sup>3</sup> | (250)        | (1.8)       |              |             |                  |             |
| Other items   | (137)        | (0.9)       | (36)         | (0.3)       | (19)             | (0.2)       |
| Overall tax expense   | <b>2,645</b> | <b>18.7</b> | <b>3,272</b> | <b>26.1</b> | <b>1,943</b>     | <b>20.3</b> |

- 1 *Low income housing tax credits are designed to encourage the provision of rental housing for low income households in the US.*
- 2 *The effect of previously unrecognised temporary differences principally relates to the recognition of capital losses.*
- 3 *The gains arising from the dilution of HSBC's interests in associates are not subject to tax, and as such there is a reconciling item which reduces the effective tax rate. See Note 19.*

[Back to Contents](#)**7 Trading assets**

|   | At<br>30 June<br>2007<br>US\$m | At<br>30 June<br>2006<br>US\$m | At<br>31 December<br>2006<br>US\$m |
|---|--------------------------------|--------------------------------|------------------------------------|
| Trading assets:                                     |                                |                                |                                    |
| not subject to repledge or resale by counterparties | 319,424                        | 226,650                        | 273,507                            |
| which may be repledged or resold by counterparties  | 105,221                        | 72,645                         | 54,640                             |
|   | <b>424,645</b>                 | <b>299,295</b>                 | <b>328,147</b>                     |
| Treasury and other eligible bills                   | 10,407                         | 12,005                         | 21,759                             |
| Debt securities                                     | 176,636                        | 146,374                        | 155,447                            |
| Equity securities                                   | 35,487                         | 23,712                         | 27,149                             |
|   | <b>222,530</b>                 | <b>182,091</b>                 | <b>204,355</b>                     |
| Loans and advances to banks                         | 95,710                         | 47,416                         | 52,006                             |
| Loans and advances to customers                     | 106,405                        | 69,788                         | 71,786                             |
|   | <b>424,645</b>                 | <b>299,295</b>                 | <b>328,147</b>                     |

The following table provides an analysis of trading securities which are valued at market value and the net gains/ (losses) resulting from trading activities:

|  | At 30 June 2007        |                             | At 30 June 2006        |                             | At 31 December 2006    |                |
|--|------------------------|-----------------------------|------------------------|-----------------------------|------------------------|----------------|
|  | Fair<br>value<br>US\$m | Gains/<br>(losses)<br>US\$m | Fair<br>value<br>US\$m | Gains/<br>(losses)<br>US\$m | Fair<br>value<br>US\$m | Gains<br>US\$m |
| US Treasury and US Government agencies | 17,687                 | 41                          | 18,138                 | 76                          | 8,348                  | 15             |
| UK Government                          | 8,980                  | 77                          | 5,000                  | 59                          | 6,176                  | 18             |
| Hong Kong Government                   | 5,773                  | (6)                         | 7,867                  | (9)                         | 8,759                  | 13             |
| Other government                       | 67,739                 | 83                          | 61,382                 | 133                         | 70,747                 | 99             |
| Asset-backed securities                | 13,801                 | (82)                        | 4,004                  | (62)                        | 15,781                 | 65             |
| Corporate debt and other securities    | 73,063                 | 271                         | 61,988                 | (117)                       | 67,395                 | 90             |
| Equity securities                      | 35,487                 | (242)                       | 23,712                 | (32)                        | 27,149                 | 2              |
|  | <b>222,530</b>         | <b>142</b>                  | <b>182,091</b>         | <b>48</b>                   | <b>204,355</b>         | <b>302</b>     |

Included within the above figures are debt securities issued by banks and other financial institutions of US\$36,012 million (30 June 2006: US\$18,993 million; 31 December 2006: US\$36,153 million).

The following table analyses trading securities between those listed on a recognised exchange and those that are unlisted:

|                            | Treasury<br>and other<br>eligible<br>bills<br>US\$m | Debt<br>securities<br>US\$m | Equity<br>securities<br>US\$m | Total<br>US\$m |
|----------------------------|---|-----------------------------|-------------------------------|----------------|
| Fair value at 30 June 2007 |   |                             |                               |                |



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|                                 |               |                |               |                |
|---------------------------------|---------------|----------------|---------------|----------------|
| Listed on a recognised exchange | <b>39</b>     | <b>124,064</b> | <b>33,727</b> | <b>157,830</b> |
| Unlisted                        | <b>10,368</b> | <b>52,572</b>  | <b>1,760</b>  | <b>64,700</b>  |
|                                 | <b>10,407</b> | <b>176,636</b> | <b>35,487</b> | <b>222,530</b> |
| Fair value at 30 June 2006      |               |                |               |                |
| Listed on a recognised exchange | 242           | 105,326        | 21,371        | 126,939        |
| Unlisted                        | 11,763        | 41,048         | 2,341         | 55,152         |
|                                 | 12,005        | 146,374        | 23,712        | 182,091        |
| Fair value at 31 December 2006  |               |                |               |                |
| Listed on a recognised exchange | 1,373         | 112,403        | 25,337        | 139,113        |
| Unlisted                        | 20,386        | 43,044         | 1,812         | 65,242         |
|                                 | 21,759        | 155,447        | 27,149        | 204,355        |

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HSBC HOLDINGS PLC

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

The following table summarises HSBC's trading portfolios by valuation methodology at 30 June 2007:

|  | Assets                  |                  | Liabilities                             |                  |
|--|-------------------------|------------------|---|------------------|
|  | Trading securities<br>% | Derivatives<br>% | Trading securities short positions<br>% | Derivatives<br>% |
| Fair value based on:   |                         |                  |   |                  |
| Quoted market prices   | 81.7                    | 1.4              | 92.5                                    | 1.8              |
| Internal models with significant observable market parameters <sup>1</sup> | 18.2                    | 96.8             | 7.5                                     | 96.3             |
| Internal models with significant unobservable market parameters            | 0.1                     | 1.8              |   | 1.9              |
|  | <b>100.0</b>            | <b>100.0</b>     | <b>100.0</b>                            | <b>100.0</b>     |

<sup>1</sup> Including investments valued on the basis of comparable investments.

**8 Financial assets designated at fair value**

|                                   | At<br>30 June<br>2007<br>US\$m | At<br>30 June<br>2006<br>US\$m | At<br>31 December<br>2006<br>US\$m |
|-----------------------------------|--------------------------------|--------------------------------|------------------------------------|
| Treasury and other eligible bills | 206                            | 80                             | 133                                |
| Debt securities                   | 15,832                         | 5,934                          | 9,449                              |
| Equity securities                 | 18,319                         | 10,240                         | 10,602                             |
|                                   | <b>34,357</b>                  | 16,254                         | 20,184                             |
| Loans and advances to banks       | 356                            | 212                            | 236                                |
| Loans and advances to customers   | 136                            | 389                            | 153                                |
|                                   | <b>34,849</b>                  | 16,855                         | 20,573                             |

The following table provides an analysis by type of issuer, excluding loans and advances:

|  | At<br>30 June<br>2007<br>US\$m | At<br>30 June<br>2006<br>US\$m | At<br>31 December<br>2006<br>US\$m |
|--|--------------------------------|--------------------------------|------------------------------------|
|  |                                |                                |                                    |

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|  |               |        |        |
|--|---------------|--------|--------|
| US Treasury and US Government agencies | <b>116</b>    | 105    | 92     |
| UK Government                          | <b>901</b>    | 1,265  | 1,359  |
| Hong Kong Government                   | <b>210</b>    | 162    | 216    |
| Other government                       | <b>2,910</b>  | 1,535  | 2,131  |
| Asset-backed securities                | <b>3,486</b>  | 320    | 274    |
| Corporate debt and other securities    | <b>8,415</b>  | 2,627  | 5,510  |
| Equity securities                      | <b>18,319</b> | 10,240 | 10,602 |
|  | <b>34,357</b> | 16,254 | 20,184 |

*Included within the above figures are debt securities issued by banks and other financial institutions of US\$8,378 million (30 June 2006: US\$2,111 million; 31 December 2006: US\$2,438 million).*

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The following table analyses securities designated at fair value between those listed on a recognised exchange and those that are unlisted:

|                                       | Treasury<br>and other<br>eligible bills<br>US\$m | Debt<br>securities<br>US\$m | Equity<br>securities<br>US\$m | Total<br>US\$m |
|---------------------------------------|--|-----------------------------|-------------------------------|----------------|
| <b>Fair value at 30 June 2007</b>     |  |                             |                               |                |
| Listed on a recognised exchange       | 83   | 7,213                       | 14,307                        | 21,603         |
| Unlisted                              | 123  | 8,619                       | 4,012                         | 12,754         |
|                                       | <u>206</u>                                       | <u>15,832</u>               | <u>18,319</u>                 | <u>34,357</u>  |
| <b>Fair value at 30 June 2006</b>     |  |                             |                               |                |
| Listed on a recognised exchange       | 80   | 3,003                       | 8,289                         | 11,372         |
| Unlisted                              |  | 2,931                       | 1,951                         | 4,882          |
|                                       | <u>80</u>  | <u>5,934</u>                | <u>10,240</u>                 | <u>16,254</u>  |
| <b>Fair value at 31 December 2006</b> |  |                             |                               |                |
| Listed on a recognised exchange       | 133  | 4,939                       | 9,212                         | 14,284         |
| Unlisted                              |  | 4,510                       | 1,390                         | 5,900          |
|                                       | <u>133</u>                                       | <u>9,449</u>                | <u>10,602</u>                 | <u>20,184</u>  |

## 9 Derivatives

Fair values of derivatives by product contract type

|                         | Assets           |                  |                | Liabilities      |                  |                  |
|-------------------------|------------------|------------------|----------------|------------------|------------------|------------------|
|                         | Trading<br>US\$m | Hedging<br>US\$m | Total<br>US\$m | Trading<br>US\$m | Hedging<br>US\$m | Total<br>US\$m   |
| <b>At 30 June 2007</b>  |                  |                  |                |                  |                  |                  |
| Foreign exchange        | 35,704           | 2,742            | 38,446         | (33,254)         | (300)            | (33,554)         |
| Interest rate           | 81,689           | 1,956            | 83,645         | (81,455)         | (1,254)          | (82,709)         |
| Equities                | 17,017           |                  | 17,017         | (16,795)         |                  | (16,795)         |
| Credit derivatives      | 9,902            |                  | 9,902          | (10,826)         |                  | (10,826)         |
| Commodity and other     | 1,028            |                  | 1,028          | (1,257)          |                  | (1,257)          |
| Gross total fair values | <u>145,340</u>   | <u>4,698</u>     | <u>150,038</u> | <u>(143,587)</u> | <u>(1,554)</u>   | <u>(145,141)</u> |
| Netting                 |                  |                  | <u>(857)</u>   |                  |                  | <u>857</u>       |
| Total                   |                  |                  | <u>149,181</u> |                  |                  | <u>(144,284)</u> |
| <b>At 30 June 2006</b>  |                  |                  |                |                  |                  |                  |
| Foreign exchange        | 25,684           | 2,374            | 28,058         | (24,635)         | (344)            | (24,979)         |
| Interest rate           | 62,965           | 1,989            | 64,954         | (64,728)         | (1,307)          | (66,035)         |
| Equities                | 9,466            |                  | 9,466          | (9,939)          |                  | (9,939)          |
| Credit derivatives      | 4,437            |                  | 4,437          | (4,587)          |                  | (4,587)          |

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|                         |         |       |         |           |         |           |
|-------------------------|---------|-------|---------|-----------|---------|-----------|
| Commodity and other     | 2,176   |       | 2,176   | (2,546)   |         | (2,546)   |
| Gross total fair values | 104,728 | 4,363 | 109,091 | (106,435) | (1,651) | (108,086) |
| Netting                 |         |       | (4,426) |           |         | 4,426     |
| Total                   |         |       | 104,665 |           |         | (103,660) |
| At 31 December 2006     |         |       |         |           |         |           |
| Foreign exchange        | 30,648  | 2,399 | 33,047  | (28,837)  | (394)   | (29,231)  |
| Interest rate           | 52,664  | 1,551 | 54,215  | (52,927)  | (1,287) | (54,214)  |
| Equities                | 10,767  |       | 10,767  | (11,647)  | (7)     | (11,654)  |
| Credit derivatives      | 8,237   |       | 8,237   | (8,611)   |         | (8,611)   |
| Commodity and other     | 1,304   |       | 1,304   | (1,636)   |         | (1,636)   |
| Gross total fair values | 103,620 | 3,950 | 107,570 | (103,658) | (1,688) | (105,346) |
| Netting                 |         |       | (3,868) |           |         | 3,868     |
| Total                   |         |       | 103,702 |           |         | (101,478) |

The definition of derivatives, HSBC's use of derivatives, and the accounting policy and presentation of derivatives are as described in the *Annual Report and Accounts 2006*.

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HSBC HOLDINGS PLC

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

## Trading derivatives

**Contractual amounts of derivatives held for trading purposes by product type**

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

|                     | At<br><b>30 June</b><br><b>2007</b><br>US\$m | At<br>30 June<br>2006<br>US\$m | At<br>31 December<br>2006<br>US\$m |
|---------------------|--|--------------------------------|------------------------------------|
| Foreign exchange    | 2,842,549                                    | 2,078,054                      | 2,182,005                          |
| Interest rate       | 10,528,816                                   | 8,436,016                      | 9,843,601                          |
| Equities            | 270,619                                      | 175,896                        | 207,016                            |
| Credit derivatives  | 1,473,509                                    | 835,944                        | 1,109,828                          |
| Commodity and other | 35,826                                       | 39,093                         | 30,532                             |
|                     | <b>15,151,319</b>                            | <b>11,565,003</b>              | <b>13,372,982</b>                  |

**Derivatives valued using models with unobservable inputs**

The amount that has yet to be recognised in the consolidated income statement relating to the difference between the fair value at initial recognition (the transaction price) and the amount that would have arisen had valuation techniques used for subsequent measurement been applied at initial recognition, less subsequent releases, is as follows:

|   | At<br><b>30 June</b><br><b>2007</b><br>US\$m | At<br>30 June<br>2006<br>US\$m | At<br>31 December<br>2006<br>US\$m |
|---|--|--------------------------------|------------------------------------|
| Unamortised balance at beginning of period            | 214  | 252                            | 237                                |
| Deferral on new transactions                          | 119  | 148                            | 135                                |
| Recognised in the income statement during the period: |  |                                |                                    |
| amortisation  | (25)   | (44)                           | (15)                               |
| subsequent to unobservable inputs becoming observable | (64)   | (110)                          | (116)                              |
| maturity or termination                               | (41)   | (16)                           | (37)                               |
| Exchange differences                                  | 1  | 7                              | 10                                 |
| Unamortised balance at end of period                  | <b>204</b>                                   | <b>237</b>                     | <b>214</b>                         |

## Hedging instruments

**Contractual amounts of derivatives held for hedging purposes by product type**

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

|                          | At<br><b>30 June</b><br><b>2007</b><br><b>US\$m</b> | At<br>30 June<br>2006<br>US\$m | At<br>31 December<br>2006<br>US\$m |
|--------------------------|---|--------------------------------|------------------------------------|
| <b>Cash flow hedges</b>  |   |                                |                                    |
| Foreign exchange         | 21,034  | 21,270                         | 21,765                             |
| Interest rate            | 213,889   | 188,827                        | 201,635                            |
|                          | <u>234,923</u>                                      | <u>210,097</u>                 | <u>223,400</u>                     |
| <b>Fair value hedges</b> |   |                                |                                    |
| Foreign exchange         | 2,998   | 2,332                          | 2,985                              |
| Interest rate            | 27,956  | 21,681                         | 24,279                             |
| Equities                 |   |                                | 30                                 |
|                          | <u>30,954</u>                                       | <u>24,013</u>                  | <u>27,294</u>                      |

### Fair value hedges

The fair values of outstanding derivatives designated as fair value hedges at 30 June 2007 were assets of US\$342 million and liabilities of US\$350 million (30 June 2006: assets of US\$285 million and liabilities of US\$414 million; 31 December 2006: assets of US\$201 million and liabilities of US\$315 million).

[Back to Contents](#)**Gains or losses arising from fair value hedges**

|   | Half-year to                      |                          |                              |
|---|-----------------------------------|--------------------------|------------------------------|
|   | <b>30 June<br/>2007<br/>US\$m</b> | 30 June<br>2006<br>US\$m | 31 December<br>2006<br>US\$m |
| Gains/(losses):                                     |                                   |                          |                              |
| on hedging instruments                              | <b>124</b>                        | 259                      | (251)                        |
| on the hedged items attributable to the hedged risk | <b>(103)</b>                      | (270)                    | 278                          |
|   | <b>21</b>                         | (11)                     | 27                           |

**Cash flow hedges**

At 30 June 2007, the fair values of outstanding derivatives designated as cash flow hedges were assets of US\$4,356 million and liabilities of US\$1,204 million (30 June 2006: assets of US\$4,078 million and liabilities of US\$1,058 million; 31 December 2006: assets of US\$3,749 million and liabilities of US\$1,364 million).

The gains and losses on ineffective portions of such derivatives are recognised immediately in the income statement. During the period to 30 June 2007, a loss of US\$49 million was recognised due to hedge ineffectiveness (first half of 2006: US\$46 million; second half of 2006: US\$76 million).

**Hedges of net investments in foreign operations**

At 30 June 2007, the fair values of outstanding financial instruments designated as hedges of net investments in foreign operations were liabilities of US\$306 million (30 June 2006: liabilities of US\$179 million; 31 December 2006: liabilities of US\$254 million).

**10 Financial investments**

|   | <b>At<br/>30 June<br/>2007<br/>US\$m</b> | At<br>30 June<br>2006<br>US\$m | At<br>31 December<br>2006<br>US\$m |
|---|--|--------------------------------|------------------------------------|
|   | Financial investments:                   |                                |                                    |
| not subject to repledge or resale by counterparties | <b>223,762</b>                           | 187,438                        | 197,055                            |
| which may be repledged or resold by counterparties  | <b>9,239</b>                             | 4,896                          | 7,751                              |
|   | <b>233,001</b>                           | 192,334                        | 204,806                            |

|                                    | At 30 June 2007             |                     | At 30 June 2006             |                     | At 31 December 2006         |                     |
|------------------------------------|-----------------------------|---------------------|-----------------------------|---------------------|-----------------------------|---------------------|
|                                    | Carrying<br>amount<br>US\$m | Fair value<br>US\$m | Carrying<br>amount<br>US\$m | Fair value<br>US\$m | Carrying<br>amount<br>US\$m | Fair value<br>US\$m |
| Treasury and other eligible bills. | <b>26,077</b>               | <b>26,077</b>       | 23,769                      | 23,769              | 25,313                      | 25,313              |
| available-for-sale                 | <b>26,077</b>               | <b>26,077</b>       | 23,658                      | 23,658              | 25,268                      | 25,268              |
| held-to-maturity                   |                             |                     | 111                         | 111                 | 45                          | 45                  |
| Debt securities                    | <b>197,621</b>              | <b>197,563</b>      | 161,583                     | 161,420             | 171,196                     | 171,498             |
| available-for-sale                 | <b>187,929</b>              | <b>187,929</b>      | 153,168                     | 153,168             | 161,870                     | 161,870             |



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|                             |                |                |         |         |         |         |
|-----------------------------|----------------|----------------|---------|---------|---------|---------|
| held-to-maturity            | <b>9,692</b>   | <b>9,634</b>   | 8,415   | 8,252   | 9,326   | 9,628   |
| Equity securities           | <b>9,303</b>   | <b>9,303</b>   | 6,982   | 6,982   | 8,297   | 8,297   |
| available-for-sale          | <b>9,303</b>   | <b>9,303</b>   | 6,982   | 6,982   | 8,297   | 8,297   |
| Total financial investments | <b>233,001</b> | <b>232,943</b> | 192,334 | 192,171 | 204,806 | 205,108 |

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HSBC HOLDINGS PLC

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

The following table analyses the carrying amount of unrealised gains and losses of financial investments:

|                                     | Cost<br>US\$m  | Gross<br>unrealised<br>gains<br>US\$m | Gross<br>unrealised<br>losses<br>US\$m | Fair<br>value<br>US\$m |
|-------------------------------------|----------------|---------------------------------------|--|------------------------|
| <b>At 30 June 2007</b>              |                |                                       |  |                        |
| US Treasury                         | 8,204          |                                       | (31)                                   | 8,173                  |
| US Government agencies              | 5,635          | 27                                    | (147)                                  | 5,515                  |
| US Government sponsored entities    | 14,331         | 32                                    | (535)                                  | 13,828                 |
| UK Government                       | 1,508          | 13                                    | (14)                                   | 1,507                  |
| Hong Kong Government                | 2,750          |                                       | (12)                                   | 2,738                  |
| Other government                    | 48,241         | 517                                   | (220)                                  | 48,538                 |
| Asset-backed securities             | 31,466         | 2                                     | (10)                                   | 31,458                 |
| Corporate debt and other securities | 112,504        | 251                                   | (872)                                  | 111,883                |
| Equities                            | 6,318          | 2,992                                 | (7)                                    | 9,303                  |
|                                     | <b>230,957</b> | <b>3,834</b>                          | <b>(1,848)</b>                         | <b>232,943</b>         |
| <b>At 30 June 2006</b>              |                |                                       |  |                        |
| US Treasury                         | 9,204          |                                       | (64)                                   | 9,140                  |
| US Government agencies              | 5,550          | 32                                    | (190)                                  | 5,392                  |
| US Government sponsored entities    | 17,166         | 23                                    | (583)                                  | 16,606                 |
| UK Government                       | 8,618          | 10                                    | (9)                                    | 8,619                  |
| Hong Kong Government                | 3,236          |                                       | (28)                                   | 3,208                  |
| Other government                    | 34,098         | 146                                   | (178)                                  | 34,066                 |
| Asset-backed securities             | 2,185          | 4                                     | (13)                                   | 2,176                  |
| Corporate debt and other securities | 106,430        | 272                                   | (720)                                  | 105,982                |
| Equities                            | 5,685          | 1,309                                 | (12)                                   | 6,982                  |
|                                     | <b>192,172</b> | <b>1,796</b>                          | <b>(1,797)</b>                         | <b>192,171</b>         |
| <b>At 31 December 2006</b>          |                |                                       |  |                        |
| US Treasury                         | 10,219         | 5                                     | (21)                                   | 10,203                 |
| US Government agencies              | 6,004          | 40                                    | (76)                                   | 5,968                  |
| US Government sponsored entities    | 14,010         | 74                                    | (285)                                  | 13,799                 |
| UK Government                       | 7,515          | 10                                    | (23)                                   | 7,502                  |
| Hong Kong Government                | 1,085          | 1                                     | (6)                                    | 1,080                  |
| Other government                    | 37,828         | 475                                   | (105)                                  | 38,198                 |
| Asset-backed securities             | 26,752         | 9                                     | (11)                                   | 26,750                 |
| Corporate debt and other securities | 93,217         | 363                                   | (269)                                  | 93,311                 |
| Equities                            | 6,295          | 2,010                                 | (8)                                    | 8,297                  |

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202,925                      2,987                      (804)                      205,108

*Included within the above figures are debt securities issued by banks and other financial institutions of US\$109,523 million (30 June 2006: US\$75,882 million; 31 December 2006: US\$86,649 million). The fair value of these at 30 June 2007 was US\$109,302 million (30 June 2006: US\$75,704 million; 31 December 2006: US\$86,596 million).*

|  | <b>Treasury<br/>and other<br/>eligible bills<br/>available-<br/>for-sale<br/>US\$m</b> | <b>Treasury<br/>and other<br/>eligible bills<br/>held-to-<br/>maturity<br/>US\$m</b> | <b>Debt<br/>securities<br/>available-<br/>for-sale<br/>US\$m</b> | <b>Debt<br/>securities<br/>held-to-<br/>maturity<br/>US\$m</b> | <b>Equity<br/>securities<br/>US\$m</b> | <b>Total<br/>US\$m</b> |
|--|--|--|--|--|--|------------------------|
| <b>Carrying amount at 30 June 2007</b> |  |  |  |  |  |                        |
| Listed on a recognised exchange        | 1,300  |  | 84,646   | 3,397  | 2,457                                  | 91,800                 |
| Unlisted                               | 24,777   |  | 103,283  | 6,295  | 6,846                                  | 141,201                |
|  | <b>26,077</b>  |  | <b>187,929</b>   | <b>9,692</b>   | <b>9,303</b>                           | <b>233,001</b>         |
| <b>Carrying amount at 30 June 2006</b> |  |  |  |  |  |                        |
| Listed on a recognised exchange        | 1,088  |  | 60,589   | 3,671  | 3,010                                  | 68,358                 |
| Unlisted                               | 22,570   | 111  | 92,579   | 4,744  | 3,972                                  | 123,976                |
|  | <b>23,658</b>  | <b>111</b>   | <b>153,168</b>   | <b>8,415</b>   | <b>6,982</b>                           | <b>192,334</b>         |

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|                                     | Treasury and other eligible bills available-for-sale<br>US\$m | Treasury and other eligible bills held-to-maturity<br>US\$m | Debt securities available-for-sale<br>US\$m | Debt securities held-to-maturity<br>US\$m | Equity securities<br>US\$m | Total<br>US\$m |
|-------------------------------------|---|---|---|---|----------------------------|----------------|
| Carrying amount at 31 December 2006 |   |   |   |   |                            |                |
| Listed on a recognised exchange     | 1,861   | 45  | 58,216                                      | 3,590                                     | 2,937                      | 66,649         |
| Unlisted                            | 23,407  |   | 103,654                                     | 5,736                                     | 5,360                      | 138,157        |
|                                     | <b>25,268</b>   | <b>45</b>   | <b>161,870</b>                              | <b>9,326</b>                              | <b>8,297</b>               | <b>204,806</b> |

The fair value of listed held-to-maturity debt securities at 30 June 2007 was US\$3,365 million (30 June 2006: US\$3,637 million; 31 December 2006: US\$3,663 million).

The maturities of debt securities at carrying value are analysed as follows:

|  | At<br>30 June<br>2007<br>US\$m | At<br>30 June<br>2006<br>US\$m | At<br>31 December<br>2006<br>US\$m |
|--|--------------------------------|--------------------------------|------------------------------------|
| Remaining contractual maturities of total debt securities: |                                |                                |                                    |
| 1 year or less   | 72,999                         | 60,236                         | 63,932                             |
| 5 years or less but over 1 year                            | 59,329                         | 55,558                         | 55,145                             |
| 10 years or less but over 5 years                          | 14,400                         | 8,513                          | 12,015                             |
| over 10 years  | 50,893                         | 37,276                         | 40,104                             |
|  | <b>197,621</b>                 | <b>161,583</b>                 | <b>171,196</b>                     |

Remaining contractual maturities of debt securities available for sale:

|                                   |                |                |                |
|-----------------------------------|----------------|----------------|----------------|
| 1 year or less                    | 72,455         | 59,760         | 63,382         |
| 5 years or less but over 1 year   | 57,561         | 53,999         | 53,497         |
| 10 years or less but over 5 years | 10,937         | 5,885          | 8,827          |
| over 10 years                     | 46,976         | 33,524         | 36,164         |
|                                   | <b>187,929</b> | <b>153,168</b> | <b>161,870</b> |

Remaining contractual maturities of debt securities held to maturity:

|                                   |              |              |              |
|-----------------------------------|--------------|--------------|--------------|
| 1 year or less                    | 544          | 476          | 550          |
| 5 years or less but over 1 year   | 1,768        | 1,559        | 1,648        |
| 10 years or less but over 5 years | 3,463        | 2,628        | 3,188        |
| over 10 years                     | 3,917        | 3,752        | 3,940        |
|                                   | <b>9,692</b> | <b>8,415</b> | <b>9,326</b> |

**11 Non-current assets held for sale**

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On 31 May 2007, HSBC entered into a contract for the sale and leaseback of the property and long leasehold land comprising 8 Canada Square, London to Metrovacesa, S.A. ( Metrovacesa ) for £1,090 million (US\$2,154 million). Under the terms of this arrangement, HSBC has leased the building back from Metrovacesa for a period of 20 years at an annual rent of £43.5 million (US\$86 million), with annual upward-only rent reviews linked to the Retail Price Index (all items) and subject to an annual maximum and minimum increase of 6 per cent and 2.5 per cent respectively. In the normal course of business, HSBC has provided finance to Metrovacesa in respect of the debt element of this transaction at arm's length market rates in the form of a 7-month bridging loan of £810 million (US\$1,601 million), secured by a charge on the property. The equity portion of £280 million (US\$553 million) was settled in cash by Metrovacesa on 31 May 2007.

The sale has not been recognised in the financial statements at 30 June 2007 because HSBC has retained a significant interest by virtue of the loan provided to part-finance the purchase of the building. Accordingly, 8 Canada Square is presented within Other assets as a non-current asset held for sale. The equity portion received from Metrovacesa is presented on the balance sheet as deferred income. It is expected that the sale will be recognised by HSBC when the bridging loan is repaid.

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**Notes on the Financial Statements (unaudited)** (continued)**12 Trading liabilities**

|   | At<br>30 June<br>2007<br>US\$m | At<br>30 June<br>2006<br>US\$m | At<br>31 December<br>2006<br>US\$m |
|---|--------------------------------|--------------------------------|------------------------------------|
| Deposits by banks                       | 53,006                         | 38,256                         | 32,040                             |
| Customer accounts                       | 123,674                        | 89,284                         | 89,166                             |
| Debt securities in issue                | 40,953                         | 28,639                         | 34,115                             |
| Other liabilities – net short positions | 95,560                         | 71,937                         | 71,287                             |
|   | <u>313,193</u>                 | <u>228,116</u>                 | <u>226,608</u>                     |

**13 Financial liabilities designated at fair value**

|   | At<br>30 June<br>2007<br>US\$m | At<br>30 June<br>2006<br>US\$m | At<br>31 December<br>2006<br>US\$m |
|---|--------------------------------|--------------------------------|------------------------------------|
| Deposits by banks and customer accounts             | 771                            | 264                            | 577                                |
| Liabilities to customers under investment contracts | 14,521                         | 11,904                         | 13,278                             |
| Debt securities in issue                            | 37,498                         | 29,695                         | 33,167                             |
| Subordinated liabilities                            | 18,575                         | 17,982                         | 18,503                             |
| Preference shares                                   | 4,601                          | 4,509                          | 4,686                              |
|   | <u>75,966</u>                  | <u>64,354</u>                  | <u>70,211</u>                      |

**14 Maturity analysis of assets and liabilities**

The following is an analysis, by remaining contractual maturities at the balance sheet date, of asset and liability line items that represent amounts expected to be recovered or settled within one year, and after one year.

Trading assets and liabilities are excluded because they are not held for collection or settlement over the period of contractual maturity.

|   | At 30 June 2007                 |                                |                |
|---|---------------------------------|--------------------------------|----------------|
|   | Due within<br>one year<br>US\$m | Due after<br>one year<br>US\$m | Total<br>US\$m |
| <b>Assets</b>                             |                                 |                                |                |
| Financial assets designated at fair value | 4,374                           | 30,475                         | 34,849         |

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|  |                |                |                  |
|--|----------------|----------------|------------------|
| Loans and advances to banks <sup>1</sup> | 208,552        | 6,093          | 214,645          |
| Loans and advances to customers          | 411,359        | 516,742        | 928,101          |
| Financial investments                    | 97,538         | 135,463        | 233,001          |
| Other financial assets                   | 21,221         | 5,490          | 26,711           |
|  | <u>743,044</u> | <u>694,263</u> | <u>1,437,307</u> |

**Liabilities**

|  |                  |                |                  |
|--|------------------|----------------|------------------|
| Deposits by banks                              | 117,183          | 11,590         | 128,773          |
| Customer accounts                              | 950,665          | 30,167         | 980,832          |
| Financial liabilities designated at fair value | 810              | 75,156         | 75,966           |
| Debt securities in issue                       | 117,530          | 111,709        | 229,239          |
| Other financial liabilities                    | 29,951           | 8,322          | 38,273           |
| Subordinated liabilities                       | 95               | 23,409         | 23,504           |
|  | <u>1,216,234</u> | <u>260,353</u> | <u>1,476,587</u> |

*For footnote, see page 149.*

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At 30 June 2006

|  | Due within<br>one year<br>US\$m | Due after<br>one year<br>US\$m | Total<br>US\$m   |
|--|---------------------------------|--------------------------------|------------------|
| <b>Assets</b>                                  |                                 |                                |                  |
| Financial assets designated at fair value      | 1,479                           | 15,376                         | 16,855           |
| Loans and advances to banks <sup>1</sup>       | 157,247                         | 5,235                          | 162,482          |
| Loans and advances to customers                | 339,403                         | 474,806                        | 814,209          |
| Financial investments                          | 84,714                          | 107,620                        | 192,334          |
| Other financial assets                         | 15,850                          | 4,206                          | 20,056           |
|  | <u>598,693</u>                  | <u>607,243</u>                 | <u>1,205,936</u> |
| <b>Liabilities</b>                             |                                 |                                |                  |
| Deposits by banks                              | 74,047                          | 9,092                          | 83,139           |
| Customer accounts                              | 808,267                         | 25,475                         | 833,742          |
| Financial liabilities designated at fair value | 8,768                           | 55,586                         | 64,354           |
| Debt securities in issue                       | 108,232                         | 101,077                        | 209,309          |
| Other financial liabilities                    | 8,651                           | 2,883                          | 11,534           |
| Subordinated liabilities                       | 321                             | 20,083                         | 20,404           |
|  | <u>1,008,286</u>                | <u>214,196</u>                 | <u>1,222,482</u> |

At 31 December 2006

|  | Due within<br>one year<br>US\$m | Due after<br>one year<br>US\$m | Total<br>US\$m   |
|--|---------------------------------|--------------------------------|------------------|
| <b>Assets</b>                                  |                                 |                                |                  |
| Financial assets designated at fair value      | 3,735                           | 16,838                         | 20,573           |
| Loans and advances to banks <sup>1</sup>       | 179,240                         | 5,965                          | 185,205          |
| Loans and advances to customers                | 360,191                         | 507,942                        | 868,133          |
| Financial investments                          | 87,848                          | 116,958                        | 204,806          |
| Other financial assets                         | 20,833                          | 6,422                          | 27,255           |
|  | <u>651,847</u>                  | <u>654,125</u>                 | <u>1,305,972</u> |
| <b>Liabilities</b>                             |                                 |                                |                  |
| Deposits by banks                              | 89,043                          | 10,651                         | 99,694           |
| Customer accounts                              | 871,881                         | 24,953                         | 896,834          |
| Financial liabilities designated at fair value | 1,410                           | 68,801                         | 70,211           |
| Debt securities in issue                       | 111,622                         | 118,703                        | 230,325          |
| Other financial liabilities                    | 25,938                          | 2,197                          | 28,135           |
| Subordinated liabilities                       | 326                             | 22,346                         | 22,672           |
|  | <u>1,100,220</u>                | <u>247,651</u>                 | <u>1,347,871</u> |



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- 1 *Loans and advances to banks include US\$176,594 million (30 June 2006: US\$122,745 million; 31 December 2006: US\$147,512 million) which is repayable on demand or at short notice.*

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HSBC HOLDINGS PLC

**Notes on the Financial Statements (unaudited)** (continued)**15 Equity****Half-year to 30 June 2007**

|   | Other reserves                         |  |  |  |   |   |  |   |   |                                | Total equity<br>US\$m |
|---|--|--|--|--|---|---|--|---|---|--------------------------------|-----------------------|
|   | Called up<br>share<br>capital<br>US\$m | Share<br>premium <sup>1</sup><br>US\$m | Retained<br>earnings <sup>2</sup><br>US\$m | Available-<br>for-sale<br>fair value<br>reserve<br>US\$m | Cash<br>flow<br>hedging<br>reserve<br>US\$m | Foreign<br>exchange<br>reserve<br>US\$m | Share-<br>based<br>payment<br>reserve<br>US\$m | Merger<br>reserve <sup>3</sup><br>US\$m | Total<br>share-<br>holders<br>equity<br>US\$m | Minority<br>interests<br>US\$m |                       |
| At 1 January  | 5,786                                  | 7,789                                  | 65,397                                     | 2,005  | (101)                                       | 4,307                                   | 2,111  | 21,058                                  | 108,352                                       | 6,576                          | 114,928               |
| Shares issued under employee share plans  | 4                                      | 114                                    |  |  |   |   |  |   | 118   |                                | 118                   |
| Shares issued in lieu of dividends and amounts arising thereon <sup>1</sup>                   | 67                                     | (69)                                   | 2,828                                      |  |   |   |  |   | 2,826   |                                | 2,826                 |
| Profit for the period   |  |  | 10,895                                     |  |   |   |  |   | 10,895  | 619                            | 11,514                |
| Dividends to shareholders   |  |  | (6,192)                                    |  |   |   |  |   | (6,192)                                       | (474)                          | (6,666)               |
| Own shares adjustment   |  |  | (587)                                      |  |   |   |  |   | (587)   |                                | (587)                 |
| Share of changes in the equity of associates and joint ventures recognised directly in equity |  |  | 186  |  |   |   |  |   | 186   |                                | 186                   |
| Actuarial gains on defined benefit plans  |  |  | 2,004                                      |  |   |   |  |   | 2,004   | 24                             | 2,028                 |
| Exchange differences  |  |  | 1,964                                      | 231  | (9)   | 13                                      | 14   |   | 2,213   | 80                             | 2,293                 |
| Fair value gains taken to equity  |  |  |  | 1,055  | 402   |   |  |   | 1,457   | 100                            | 1,557                 |

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|  |         |       |        |       |       |       |       |         |         |         |         |
|--|---------|-------|--------|-------|-------|-------|-------|---------|---------|---------|---------|
| Amounts transferred to the income statement  |         |       | (775)  | (576) |       |       |       | (1,351) |         | (1,351) |         |
| Exercise of HSBC share awards  | 477     |       |        |       | (443) |       | 34    |         |         | 34      |         |
| Charge to the income statement in respect of equity settled share-based payments           |         |       |        |       | 413   |       | 413   |         |         | 413     |         |
| Other movements  | (119)   | (12)  | (2)    |       | (1)   |       | (134) | (113)   |         | (247)   |         |
| Tax on items taken directly to or transferred from equity                                  | (638)   | 130   | 54     |       |       |       | (454) | (1)     |         | (455)   |         |
| Transfers  | (1,964) | (231) | 9      | 2,200 | (14)  |       |       |         |         |         |         |
| Net decrease in minority interests arising on acquisitions, disposals and capital issuance |         |       |        |       |       |       |       |         | (100)   | (100)   |         |
| At 30 June   | 5,857   | 7,834 | 74,251 | 2,403 | (223) | 6,520 | 2,080 | 21,058  | 119,780 | 6,711   | 126,491 |

- 1 Share premium includes the deduction of US\$2 million issue costs incurred during the period.
- 2 Retained earnings include US\$2,400 million of own shares held within HSBC's insurance business, its retirement funds for the benefit of policyholders or beneficiaries within employee trusts, for the settlement of shares expected to be delivered under employee share schemes or bonus plans, and the market-making activities in Global Markets.
- 3 Statutory share premium relief under Section 131 of the Companies Act 1985 was taken in respect of the acquisition of HSBC Bank plc in 1992, HSBC France in 2000 and HSBC Finance Corporation in 2003 and the shares issued were recorded at their nominal value only. In HSBC's consolidated accounts the fair value difference of US\$8,290 million in respect of HSBC France and US\$12,768 million in respect of HSBC Finance Corporation is reported as a merger reserve.

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Half-year to 30 June 2006

|   | Other reserves                |                       |                           |   |                                 |                                |                                   |                        |                                  |                          |                    |
|---|-------------------------------|-----------------------|---------------------------|---|---------------------------------|--------------------------------|-----------------------------------|------------------------|----------------------------------|--------------------------|--------------------|
|   | Called up share capital US\$m | Share premium 1 US\$m | Retained earnings 2 US\$m | Available-for-sale fair value reserve US\$m | Cash flow hedging reserve US\$m | Foreign exchange reserve US\$m | Share-based payment reserve US\$m | Merger reserve 3 US\$m | Total share-holders equity US\$m | Minority interests US\$m | Total equity US\$m |
| At 1 January  | 5,667                         | 6,896                 | 56,223                    | 1,104                                       | 233                             | (284)                          | 1,535                             | 21,058                 | 92,432                           | 5,794                    | 98,226             |
| Shares issued under employee share plans  | 16                            | 398                   |                           |   |                                 |                                |                                   |                        | 414                              |                          | 414                |
| Shares issued in lieu of dividends and amounts arising thereon <sup>1</sup>                   | 58                            | (58)                  | 1,790                     |   |                                 |                                |                                   |                        | 1,790                            |                          | 1,790              |
| Profit for the period   |                               |                       | 8,729                     |   |                                 |                                |                                   |                        | 8,729                            | 516                      | 9,245              |
| Dividends to shareholders   |                               |                       | (5,270)                   |   |                                 |                                |                                   |                        | (5,270)                          | (459)                    | (5,729)            |
| Own shares adjustment   |                               |                       | (670)                     |   |                                 |                                |                                   |                        | (670)                            |                          | (670)              |
| Share of changes in the equity of associates and joint ventures recognised directly in equity |                               |                       | (44)                      |   |                                 |                                |                                   |                        | (44)                             |                          | (44)               |
| Actuarial gains on defined benefit plans  |                               |                       | 1,477                     |   |                                 |                                |                                   |                        | 1,477                            |                          | 1,477              |
| Exchange differences  |                               |                       | 2,615                     | 56  | (2)                             | 443                            | 8                                 |                        | 3,120                            | 83                       | 3,203              |
| Fair value gains/(losses) taken to equity   |                               |                       |                           | (482)                                       | 153                             |                                |                                   |                        | (329)                            |                          | (329)              |
| Amounts transferred to the income statement   |                               |                       |                           | (283)                                       | (180)                           |                                |                                   |                        | (463)                            | (33)                     | (496)              |
| Exercise of HSBC share awards   |                               |                       | 306                       |   |                                 |                                | (258)                             |                        | 48                               |                          | 48                 |
| Charge to the income statement in respect of  |                               |                       |                           |   |                                 |                                | 408                               |                        | 408                              |                          | 408                |

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|  |         |       |        |       |       |       |       |        |         |       |         |
|--|---------|-------|--------|-------|-------|-------|-------|--------|---------|-------|---------|
| equity settled share-based payments  |         |       |        |       |       |       |       |        |         |       |         |
| Other movements  | (111)   | (20)  | 58     |       | 10    |       | (63)  | (189)  | (252)   |       |         |
| Tax on items taken directly to or transferred from equity                                  | (514)   | 295   | 21     |       |       |       | (198) | 2      | (196)   |       |         |
| Transfers  | (2,521) | (30)  | 2      | 2,677 | (128) |       |       |        |         |       |         |
| Net increase in minority interests arising on acquisitions, disposals and capital issuance |         |       |        |       |       |       |       |        |         | 275   | 275     |
| At 30 June   | 5,741   | 7,236 | 62,010 | 640   | 285   | 2,836 | 1,575 | 21,058 | 101,381 | 5,989 | 107,370 |

- 1 *Share premium includes the deduction of US\$1 million issue costs incurred during the period.*
- 2 *Retained earnings include US\$2,269 million of own shares held within HSBC's insurance business, its retirement funds for the benefit of policyholders or beneficiaries within employee trusts, for the settlement of shares expected to be delivered under employee share schemes or bonus plans, and the market-making activities in Global Markets.*
- 3 *Statutory share premium relief under Section 131 of the Companies Act 1985 was taken in respect of the acquisition of HSBC Bank plc in 1992, HSBC France in 2000 and HSBC Finance Corporation in 2003 and the shares issued were recorded at their nominal value only. In HSBC's consolidated accounts the fair value difference of US\$8,290 million in respect of HSBC France and US\$12,768 million in respect of HSBC Finance Corporation is reported as a merger reserve.*

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HSBC HOLDINGS PLC

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

Half-year to 31 December 2006

|   | Other reserves                   |                                     |   |  |                                    |                                   |                                      |                                      |                                     |                             |                       |
|---|----------------------------------|-------------------------------------|---|--|------------------------------------|-----------------------------------|--------------------------------------|--------------------------------------|-------------------------------------|-----------------------------|-----------------------|
|   | Called up share capital<br>US\$m | Share premium <sup>1</sup><br>US\$m | Retained earnings <sup>2</sup><br>US\$m | Available-for-sale fair value reserve<br>US\$m | Cash flow hedging reserve<br>US\$m | Foreign exchange reserve<br>US\$m | Share-based payment reserve<br>US\$m | Merger reserve <sup>3</sup><br>US\$m | Total share-holders equity<br>US\$m | Minority interests<br>US\$m | Total equity<br>US\$m |
| At 1 July   | 5,741                            | 7,236                               | 62,010                                  | 640  | 285                                | 2,836                             | 1,575                                | 21,058                               | 101,381                             | 5,989                       | 107,370               |
| Shares issued under employee share plans  | 24                               | 577                                 |   |  |                                    |                                   |                                      |                                      | 601                                 |                             | 601                   |
| Shares issued in lieu of dividends and amounts arising thereon <sup>1</sup>                   | 21                               | (24)                                | 738                                     |  |                                    |                                   |                                      |                                      | 735                                 |                             | 735                   |
| Profit for the period   |                                  |                                     | 7,060                                   |  |                                    |                                   |                                      |                                      | 7,060                               | 566                         | 7,626                 |
| Dividends to shareholders   |                                  |                                     | (3,499)                                 |  |                                    |                                   |                                      |                                      | (3,499)                             | (326)                       | (3,825)               |
| Own shares adjustment   |                                  |                                     | 141                                     |  |                                    |                                   |                                      |                                      | 141                                 |                             | 141                   |
| Share of changes in the equity of associates and joint ventures recognised directly in equity |                                  |                                     | 64                                      |  |                                    |                                   |                                      |                                      | 64                                  |                             | 64                    |
| Actuarial losses on defined benefit plans   |                                  |                                     | (1,569)                                 |  |                                    |                                   |                                      |                                      | (1,569)                             | 14                          | (1,555)               |
| Exchange differences  |                                  |                                     | 1,831                                   | 33   | (6)                                | (417)                             | 30                                   |                                      | 1,471                               | 1                           | 1,472                 |
| Fair value gains taken to equity  |                                  |                                     |   | 1,996  | 1,407                              |                                   |                                      |                                      | 3,403                               | 62                          | 3,465                 |
| Amounts transferred to the income   |                                  |                                     |   | (318)  | (2,039)                            |                                   |                                      |                                      | (2,357)                             | 11                          | (2,346)               |

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|  |         |       |        |       |       |       |       |        |         |       |         |
|--|---------|-------|--------|-------|-------|-------|-------|--------|---------|-------|---------|
| statement  |         |       |        |       |       |       |       |        |         |       |         |
| Exercise of HSBC share awards  | 378     |       |        |       | (365) |       |       | 13     |         |       | 13      |
| Charge to the income statement in respect of equity settled share-based payments           |         |       |        |       | 446   |       |       | 446    |         |       | 446     |
| Other movements  | 9       | 11    | (56)   |       | 335   |       |       | 299    | 86      |       | 385     |
| Tax on items taken directly to or transferred from equity                                  | 159     | (298) | 302    |       |       |       |       | 163    | (11)    |       | 152     |
| Transfers  | (1,925) | (59)  | 6      | 1,888 | 90    |       |       |        |         |       |         |
| Net increase in minority interests arising on acquisitions, disposals and capital issuance |         |       |        |       |       |       |       |        |         | 184   | 184     |
| At 31 December   | 5,786   | 7,789 | 65,397 | 2,005 | (101) | 4,307 | 2,111 | 21,058 | 108,352 | 6,576 | 114,928 |

- 1 Share premium includes the deduction of US\$2 million issue costs incurred during the period.
- 2 Retained earnings include US\$2,107 million of own shares held within HSBC's insurance business, its retirement funds for the benefit of policyholders or beneficiaries within employee trusts, for the settlement of shares expected to be delivered under employee share schemes or bonus plans, and the market-making activities in Global Markets.
- 3 Statutory share premium relief under Section 131 of the Companies Act 1985 was taken in respect of the acquisition of HSBC Bank plc in 1992, HSBC France in 2000 and HSBC Finance Corporation in 2003 and the shares issued were recorded at their nominal value only. In HSBC's consolidated accounts the fair value difference of US\$8,290 million in respect of HSBC France and US\$12,768 million in respect of HSBC Finance Corporation is reported as a merger reserve.

[Back to Contents](#)**16 Notes on the cash flow statement**

|  | Half-year<br>to          |                          |                                 |
|--|--------------------------|--------------------------|---------------------------------|
|  | 30 June<br>2007<br>US\$m | 30 June<br>2006<br>US\$m | 31<br>December<br>2006<br>US\$m |
| <b>(a) Non-cash items included in profit before tax</b>  |                          |                          |                                 |
| Depreciation and amortisation                            | 1,184                    | 1,085                    | 1,443                           |
| Revaluation of investment properties                     | (48)                     | (80)                     | (84)                            |
| Share-based payment expense                              | 413                      | 408                      | 446                             |
| Loan impairment losses gross of recoveries               | 6,635                    | 4,233                    | 7,098                           |
| Provisions for liabilities and charges                   | 282                      | 187                      | 311                             |
| Impairment of financial investments                      | 18                       | 1                        | 20                              |
| Charge for post-employment defined benefit plans         | 342                      | 292                      | 372                             |
| Accretion of discounts and amortisation of premiums      | (392)                    | (445)                    | (331)                           |
|  | <b>8,434</b>             | <b>5,681</b>             | <b>9,275</b>                    |
| <b>(b) Change in operating assets</b>                    |                          |                          |                                 |
| Change in prepayments and accrued income                 | (2,280)                  | (1,812)                  | (666)                           |
| Change in net trading securities and net derivatives     | 10,487                   | (7,879)                  | (5,741)                         |
| Change in loans and advances to banks                    | (357)                    | (14,273)                 | 2,768                           |
| Change in loans and advances to customers                | (66,739)                 | (78,147)                 | (54,840)                        |
| Change in financial assets designated at fair value      | (5,872)                  | (1,809)                  | (3,074)                         |
| Change in other assets                                   | (924)                    | (2,293)                  | (5,503)                         |
|  | <b>(65,685)</b>          | <b>(106,213)</b>         | <b>(67,056)</b>                 |
| <b>(c) Change in operating liabilities</b>               |                          |                          |                                 |
| Change in accruals and deferred income                   | 547                      | (116)                    | 3,665                           |
| Change in deposits by banks                              | 29,661                   | 13,514                   | 14,864                          |
| Change in customer accounts                              | 84,496                   | 93,490                   | 56,359                          |
| Change in debt securities in issue                       | (1,086)                  | 21,236                   | 21,017                          |
| Change in financial liabilities designated at fair value | 5,755                    | 2,525                    | 5,857                           |
| Change in other liabilities                              | 3,875                    | 5,535                    | (568)                           |
|  | <b>123,248</b>           | <b>136,184</b>           | <b>101,194</b>                  |
| <b>(d) Cash and cash equivalents comprise</b>            |                          |                          |                                 |
| Cash and balances at central banks                       | 16,651                   | 24,343                   | 12,732                          |



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|  |                 |         |          |
|--|-----------------|---------|----------|
| Items in the course of collection from other banks                             | <b>23,152</b>   | 12,425  | 14,144   |
| Loans and advances to banks of one month or less                               | <b>220,136</b>  | 122,745 | 162,998  |
| Treasury bills, other bills and certificates of deposit less than three months | <b>32,684</b>   | 28,645  | 38,237   |
| Less: items in the course of transmission to other banks                       | <b>(20,339)</b> | (9,532) | (12,625) |
|  | <b>272,284</b>  | 178,626 | 215,486  |

Total interest paid by HSBC during the half-year was US\$31,002 million (first half of 2006: US\$21,457 million; second half of 2006: US\$26,337 million). Total interest received by HSBC during the half-year was US\$47,423 million (first half of 2006: US\$39,611 million; second half of 2006: US\$45,532 million). Total dividends received by HSBC during the half-year were US\$1,426 million (first half of 2006: US\$843 million; second half of 2006: US\$682 million).

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**Notes on the Financial Statements (unaudited)** (continued)**17 Contingent liabilities, contractual commitments and financial guarantee contracts**

|  | At<br>30 June<br>2007<br>US\$m | At<br>30 June<br>2006<br>US\$m | At<br>31<br>December<br>2006<br>US\$m |
|--|--------------------------------|--------------------------------|---------------------------------------|
| <b>Contingent liabilities and financial guarantee contracts</b>                            |                                |                                |                                       |
| Guarantees and irrevocable letters of credit pledged as collateral security <sup>1</sup> : |                                |                                |                                       |
| 1 year and under   | 37,142                         | 41,455                         | 42,427                                |
| over 1 year  | 34,109                         | 36,222                         | 34,983                                |
| Other contingent liabilities   | 297                            | 228                            | 330                                   |
|  | <u>71,548</u>                  | <u>77,905</u>                  | <u>77,740</u>                         |
| <b>Commitments</b>   |                                |                                |                                       |
| Documentary credits and short-term trade-related transactions                              | 11,827                         | 10,105                         | 9,659                                 |
| Forward asset purchases and forward deposits placed  | 734                            | 3,124                          | 2,077                                 |
| Undrawn note issuing and revolving underwriting facilities                                 | 37                             | 370                            | 213                                   |
| Undrawn formal standby facilities, credit lines and other commitments to lend:             |                                |                                |                                       |
| 1 year and under   | 621,158                        | 548,375                        | 584,167                               |
| over 1 year  | 130,214                        | 110,032                        | 118,514                               |
|  | <u>763,970</u>                 | <u>672,006</u>                 | <u>714,630</u>                        |

<sup>1</sup> Including financial guarantee contracts.

The above table discloses the nominal principal amounts of third party off-balance sheet transactions, the amounts relating to other contingent liabilities and the nominal principal amounts relating to financial guarantee contracts.

Contingent liabilities and commitments are mainly credit-related instruments which include non-financial guarantees and commitments to extend credit. Contractual amounts represent the amounts at risk should contracts be fully drawn upon and clients default. Since a significant portion of guarantees and commitments are expected to expire without being drawn upon, the total of the contractual amounts is not representative of future liquidity requirements.

**18 Segmental analysis**

Net operating income and profit before tax is presented below by geography, HSBC's primary basis of segmental reporting.

Net operating income

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|                      | <b>Europe</b> | <b>Hong</b>  | <b>Rest of</b> | <b>North</b>   | <b>Latin</b>   | <b>Intra-</b> | <b>Total</b>  |
|----------------------|---------------|--------------|----------------|----------------|----------------|---------------|---------------|
|                      | <b>US\$m</b>  | <b>Kong</b>  | <b>Asia-</b>   | <b>America</b> | <b>America</b> | <b>HSBC</b>   | <b>US\$m</b>  |
|                      |               | <b>US\$m</b> | <b>Pacific</b> | <b>l</b>       | <b>l</b>       | <b>items</b>  |               |
|                      |               |              | <b>US\$m</b>   | <b>US\$m</b>   | <b>US\$m</b>   | <b>US\$m</b>  | <b>US\$m</b>  |
| <b>Half-year to:</b> |               |              |                |                |                |               |               |
| <b>30 June 2007</b>  | <b>11,934</b> | <b>4,982</b> | <b>4,912</b>   | <b>7,660</b>   | <b>3,511</b>   | <b>(852)</b>  | <b>32,147</b> |
| 30 June 2006         | 10,389        | 4,148        | 2,880          | 8,684          | 2,811          | (617)         | 28,295        |
| 31 December 2006     | 10,528        | 4,284        | 3,330          | 6,147          | 3,086          | (877)         | 26,498        |

Profit before tax

|                      | <b>Europe</b> | <b>Hong</b>  | <b>Rest of</b> | <b>North</b>   | <b>Latin</b>   | <b>Intra-</b> | <b>Total</b>  |
|----------------------|---------------|--------------|----------------|----------------|----------------|---------------|---------------|
|                      | <b>US\$m</b>  | <b>Kong</b>  | <b>Asia-</b>   | <b>America</b> | <b>America</b> | <b>HSBC</b>   | <b>US\$m</b>  |
|                      |               | <b>US\$m</b> | <b>Pacific</b> | <b>l</b>       | <b>l</b>       | <b>items</b>  |               |
|                      |               |              | <b>US\$m</b>   | <b>US\$m</b>   | <b>US\$m</b>   | <b>US\$m</b>  | <b>US\$m</b>  |
| <b>Half-year to:</b> |               |              |                |                |                |               |               |
| <b>30 June 2007</b>  | <b>4,050</b>  | <b>3,330</b> | <b>3,344</b>   | <b>2,435</b>   | <b>1,000</b>   |               | <b>14,159</b> |
| 30 June 2006         | 3,600         | 2,654        | 1,657          | 3,741          | 865            |               | 12,517        |
| 31 December 2006     | 3,374         | 2,528        | 1,870          | 927            | 870            |               | 9,569         |

1 In 2006, Mexico and Panama were reclassified from the North America segment to the Latin America segment. Comparative information has been restated accordingly.

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## 19 Gains from dilution of interests in associates

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During the first half of 2007, three of HSBC's associates, Industrial Bank, Ping An Insurance and Bank of Communications, issued new shares. HSBC did not subscribe for any of the shares issued under these offers and, as a result, its interests in the associates' equity decreased from 15.98 per cent to 12.78 per cent, from 19.90 per cent to 16.78 per cent and from 19.90 per cent to 18.60 per cent, respectively.

The assets of each associate substantially increased as a result of the new share issues and, as a consequence, the transactions resulted in an increase of US\$1,076 million in HSBC's share of the associates' underlying net assets, notwithstanding the reduction in the Group's interests. This increase represents gains from dilution of the Group's interests in the associates, and is presented in the income statement.

The dilution of the interests does not affect the classification of the Group's investments as investments in associates.

The gains resulting from the dilution of HSBC's interests in the associates were US\$187 million, US\$485 million and US\$404 million in respect of Industrial Bank, Ping An Insurance and Bank of Communications, respectively. The gain relating to Industrial Bank includes a minority interest gain of US\$71 million.

## 20 Litigation

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On 27 July 2007, the UK Office of Fair Trading issued High Court legal proceedings against a number of UK financial institutions, including HSBC Bank plc, to determine the legal status and enforceability of certain of the charges applied to their personal customers in relation to unauthorised overdrafts (the Charges). The proceedings were commenced with the agreement of all parties concerned. Proceedings are at a very early stage, and may (if appeals are pursued) take a number of years to conclude. A range of outcomes is possible, depending upon the Court's assessment of each Charge across the period under review. HSBC Bank plc considers the Charges to be and to have been valid and enforceable, and intends strongly to defend its position. It is impossible at this stage to predict accurately the outcome of the litigation or whether the proceedings will have any financial impact and, if so, the size of that impact but on the basis of facts currently available and the advice received the financial impact on HSBC is not considered to be material.

HSBC is party to legal actions in a number of jurisdictions including the UK, Hong Kong and the US, arising out of its normal business operations. HSBC considers that none of the actions is regarded as material, and none is expected to result in a significant adverse effect on the financial position of HSBC, either individually or in the aggregate. Management believes that adequate provisions have been made in respect of such litigation. HSBC has not disclosed any contingent liability associated with these legal actions in aggregate because it is not practicable to do so.

## 21 Interim Report 2007 and statutory accounts

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The information in this *Interim Report 2007* is unaudited and does not constitute statutory accounts within the meaning of section 240 of the Companies Act 1985 (the Act). The *Interim Report 2007* was approved by the Board of Directors on 30 July 2007. The statutory accounts for the year ended 31 December 2006 have been delivered to the Registrar of Companies in England and Wales in accordance with section 242 of the Act. The auditor has reported on those accounts. Its report was unqualified and did not contain a statement under section 237(2) or (3) of the Act.

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**Additional Information****1 Directors interests**

According to the register of Directors interests maintained by HSBC Holdings pursuant to section 352 of the Securities and Futures Ordinance of Hong Kong, the Directors of HSBC Holdings at 30 June 2007 had the following interests, all beneficial unless otherwise stated, in the shares and loan capital of HSBC and its associates:

*HSBC Holdings ordinary shares of US\$0.50*

|                       | At 30 June 2007         |                     |                                |                           |                        |                                      |                                 |   |
|-----------------------|-------------------------|---------------------|--------------------------------|---------------------------|------------------------|--------------------------------------|---------------------------------|---|
|                       | At<br>1 January<br>2007 | Beneficial<br>owner | Child<br>under 18<br>or spouse | Controlled<br>corporation | Trustee                | Jointly<br>with<br>another<br>person | Total<br>interests <sup>1</sup> | Percentage<br>of ordinary<br>shares<br>in issue |
| J D Coombe            | 39,799                  | 12,295              |                                |                           | 33,799 <sub>2</sub>    |                                      | 46,094                          | 0.00  |
| Baroness Dunn         | 176,525                 | 152,126             |                                |                           | 28,650 <sub>2</sub>    |                                      | 180,776                         | 0.00  |
| D J Flint             | 104,947                 | 79,269              |                                |                           | 28,767 <sub>3</sub>    |                                      | 108,036                         | 0.00  |
| W K L Fung            | 328,000                 | 328,000             |                                |                           |                        |                                      | 328,000                         | 0.00  |
| M F Geoghegan         | 113,525                 | 380,973             |                                |                           |                        |                                      | 380,973                         | 0.00  |
| S K Green             | 401,796                 | 482,377             |                                |                           |                        | 45,355                               | 527,732                         | 0.00  |
| J W J Hughes-Hallett  | 1,668,986               |                     |                                |                           | 1,288,007 <sub>2</sub> |                                      | 1,288,007                       | 0.01  |
| Sir Brian Moffat      | 12,149                  |                     |                                |                           |                        | 17,498                               | 17,498                          | 0.00  |
| Sir Mark Moody-Stuart | 10,840                  | 5,000               | 840                            |                           | 5,000 <sub>2</sub>     |                                      | 10,840                          | 0.00  |
| S W Newton            | 5,631                   | 5,793               |                                | 50,000                    |                        |                                      | 55,793                          | 0.00  |
| S M Robertson         | 38,976                  | 5,218               |                                |                           |                        |                                      | 5,218                           | 0.00  |
| Sir Brian Williamson  | 17,281                  | 22,778              |                                |                           |                        |                                      | 22,778                          | 0.00  |

<sup>1</sup> *Details of executive Directors other interests in HSBC Holdings ordinary shares of US\$0.50 arising from the HSBC Holdings Savings-Related Share Option Plan, the HSBC Holdings Restricted Share Plan 2000 and The HSBC Share Plan are set out on the following pages. At 30 June 2007, the aggregate interests under the Securities and Futures Ordinance of Hong Kong of D J Flint, M F Geoghegan and S K Green in HSBC Holdings ordinary shares of US\$0.50 (each of which represents less than 0.02 per cent of the shares in issue), including interests arising through employee share plans were: D J Flint 861,065; M F Geoghegan 1,484,304; and S K Green 1,680,133.*

<sup>2</sup> *Non-beneficial.*

<sup>3</sup> *Non-beneficial interest in 9,589 HSBC Holdings ordinary shares of US\$0.50.*

M F Geoghegan has an interest as beneficial owner in 280,000 ordinary shares of HK\$5.00 each in Hang Seng Bank Limited (representing less than 0.02 per cent of the shares in issue), which he acquired during the period. S K Green has an interest as beneficial owner in 75,000 of HSBC Holdings plc 5½ per cent Subordinated Notes 2009, which he held throughout the period.

As Directors of HSBC France, S K Green and M F Geoghegan each have an interest as beneficial owner in one share of 5 in that company (representing less than 0.01 per cent of the shares in issue), which they held throughout the period. The Directors have waived their rights to receive dividends on these shares and have undertaken to transfer these shares to HSBC on ceasing to be Directors of HSBC France.

As a Director of HSBC Private Banking Holdings (Suisse) SA, S K Green has an interest as beneficial owner in one share of CHF1,000 in that company (representing less than 0.01 per cent of the shares in issue), which he held throughout the period. S K Green has waived his rights to receive dividends on the share and has undertaken to transfer the share to HSBC on ceasing to be a Director of HSBC Private Banking Holdings (Suisse) SA.

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### HSBC Holdings Savings-Related Share Option Plan

*HSBC Holdings ordinary shares of US\$0.50*

|           | Date of award | Exercise price (£) | Exercisable from <sup>1</sup> | Exercisable until | Options held at 1 January 2007 | Options awarded during period | Options held at 30 June 2007 |
|-----------|---------------|--------------------|-------------------------------|-------------------|--------------------------------|-------------------------------|------------------------------|
| D J Flint | 2 May 2002    | 6.3224             | 1 Aug 2007                    | 31 Jan 2008       | 2,617                          |                               | 2,617                        |
|           | 25 Apr 2007   | 7.0872             | 1 Aug 2012                    | 31 Jan 2013       |                                | 2,310                         | 2,310                        |
| S K Green | 23 Apr 2003   | 5.3496             | 1 Aug 2008                    | 31 Jan 2009       | 3,070                          |                               | 3,070                        |

*The options were awarded for nil consideration and are exercisable at a 20 per cent discount to the average market value of the ordinary shares on the five business days immediately preceding the invitation date. The market value of the ordinary shares at 30 June 2007 was £9.15. The highest and lowest market values during the period were £9.555 and £8.80. Market value is the mid-market price derived from the London Stock Exchange Daily Official List on the relevant date. Under the Securities and Futures Ordinance of Hong Kong, the options are categorised as unlisted physically settled equity derivatives.*

<sup>1</sup> May be advanced to an earlier date in certain circumstances, e.g. retirement.

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**Additional Information** (continued)

## HSBC Holdings Restricted Share Plan 2000

*HSBC Holdings ordinary shares of US\$0.50*

|               | Date of award | Year in which awards may vest | Awards held at 1 January 2007 | Awards vested during period <sup>1</sup> | Monetary value of awards vested during period £000 | Awards held at 30 June 2007 <sup>1</sup> |
|---------------|---------------|-------------------------------|-------------------------------|--|--|--|
| D J Flint     | 8 Mar 2002    | 2007                          | 90,176                        | 90,9872                                  | 830  |  |
|               | 5 Mar 2003    | 2008                          | 129,917                       |  |  | 133,653                                  |
|               | 4 Mar 2004    | 2009                          | 136,357                       |  |  | 3  |
| M F Geoghegan | 8 Mar 2002    | 2007                          | 45,089                        | 45,4492                                  | 414  |  |
|               | 5 Mar 2003    | 2008                          | 60,630                        |  |  | 62,373                                   |
|               | 4 Mar 2004    | 2009                          | 102,268                       |  |  | 3  |
| S K Green     | 8 Mar 2002    | 2007                          | 112,720                       | 113,6212                                 | 1,036  |  |
|               | 5 Mar 2003    | 2008                          | 129,917                       |  |  | 133,653                                  |
|               | 4 Mar 2004    | 2009                          | 187,490                       |  |  | 3  |

*Vesting of these awards is subject to the performance conditions described on page 289 of the Annual Report and Accounts 2006. Under the Securities and Futures Ordinance of Hong Kong, interests held through the HSBC Holdings Restricted Share Plan 2000 are categorised as the interests of a beneficiary of a trust.*

- <sup>1</sup> Includes additional shares arising from scrip dividends.
- <sup>2</sup> The performance conditions have been met and the shares have vested. At the date of vesting, 8 March 2007, the market value per share was £9.12. At the date of the award, 8 March 2002, the market value per share was £8.34.
- <sup>3</sup> The performance conditions for awards made in 2004 were not met and, under the rules of the Plan, the awards held by D J Flint (137,447 shares), M F Geoghegan (103,086 shares) and S K Green (188,990 shares) were forfeited on 4 April 2007.

## The HSBC Share Plan

*HSBC Holdings ordinary shares of US\$0.50*

|           | Date of award | Year in which awards may vest | Awards held at 1 January 2007 | Awards made during period <sup>1</sup> | Monetary value of awards made during period £000 | Awards held at 30 June 2007 <sup>2</sup> |
|-----------|---------------|-------------------------------|-------------------------------|--|--|--|
| D J Flint | 27 May 2005   | 2008                          | 185,821                       |  |  | 191,165                                  |
|           |               | 2009                          | 167,220                       |  |  | 172,028                                  |



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|               |                |      |         |         |       |         |
|---------------|----------------|------|---------|---------|-------|---------|
|               | 6 Mar<br>2006  |      |         |         |       |         |
|               | 5 Mar<br>2007  | 2010 |         | 246,185 | 2,200 | 251,256 |
| M F Geoghegan | 27 May<br>2005 | 2008 | 247,761 |         |       | 254,886 |
|               | 6 Mar<br>2006  | 2009 | 209,025 |         |       | 215,036 |
|               | 5 Mar<br>2007  | 2010 |         | 559,513 | 5,000 | 571,036 |
| S K Green     | 27 May<br>2005 | 2008 | 309,701 |         |       | 318,607 |
|               | 6 Mar<br>2006  | 2009 | 261,280 |         |       | 268,794 |
|               | 5 Mar<br>2007  | 2010 |         | 419,635 | 3,750 | 428,277 |

*Vesting of these awards is subject to the performance conditions described on pages 281-283 of the Annual Report and Accounts 2006. Under the Securities and Futures Ordinance of Hong Kong, interests held through The HSBC Share Plan are categorised as the interests of a beneficiary of a trust.*

1 *At the date of the award, 5 March 2007, the market value per share was £8.96. The shares acquired by the Trustee of the Plan were purchased at an average price of £8.936358.*

2 *Includes additional shares arising from scrip dividends.*

No Directors held any short position as defined in the Securities and Futures Ordinance of Hong Kong in the shares and loan capital of HSBC and its associated corporations. Save as stated above, none of the Directors had an interest in any shares or debentures of HSBC or any associated corporation at the beginning or at the end of the period, and none of the Directors or members of their immediate family was awarded or exercised any right to subscribe for any shares or debentures in any HSBC corporation during the period.

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Since the end of the period, the interests of each of the following Directors have increased by the number of HSBC Holdings ordinary shares shown against their name:

|                      | Beneficial<br>owner | Controlled<br>corporation | Trustee | Jointly with<br>another<br>person | Beneficiary<br>of a trust |
|----------------------|---------------------|---------------------------|---------|-----------------------------------|---------------------------|
| J D Coombe           | 1131                |                           |         |                                   |                           |
| Baroness Dunn        | 1,4011              |                           |         |                                   |                           |
| D J Flint            | 7292                |                           | 2651    |                                   | 6,8973                    |
| M F Geoghegan        | 2,0461              |                           |         |                                   | 10,1723                   |
| S K Green            | 4,2884              |                           |         |                                   | 10,5963                   |
| Sir Brian Moffat     |                     |                           |         | 1151                              |                           |
| S W Newton           | 541                 | 4611                      |         |                                   |                           |
| S M Robertson        | 481                 |                           |         |                                   |                           |
| Sir Brian Williamson | 1641                |                           |         |                                   |                           |

- 1 *Scrip dividend.*
- 2 *Comprises scrip dividend on shares held as beneficial owner (674 shares), the automatic reinvestment of dividend income by an Individual Savings Account or Personal Equity Plan manager (45 shares) and the automatic reinvestment of dividend income on shares held in the HSBC Holdings UK Share Ownership Plan (10 shares).*
- 3 *Scrip dividend on awards held under the HSBC Holdings Restricted Share Plan 2000 and The HSBC Share Plan.*
- 4 *Comprises scrip dividend on shares held as beneficial owner (4,278 shares) and the automatic reinvestment of dividend income on shares held in the HSBC Holdings UK Share Ownership Plan (10 shares).*

## 2 Employee share plans

To help align the interests of employees with those of shareholders, share options are granted under all-employee share plans and discretionary awards of Performance Shares and Restricted Shares made under The HSBC Share Plan. There have been no awards of discretionary options since 30 September 2005. The following are particulars of outstanding employee share options, including those held by employees working under employment contracts that are regarded as continuous contracts for the purposes of the Hong Kong Employment Ordinance. The options were granted at nil consideration. No options have been granted to substantial shareholders, suppliers of goods or services, or in excess of the individual limit for each share plan. No options were cancelled during the period. The options which were awarded, exercised or lapsed during the period are detailed in the tables below. Particulars of options held by Directors of HSBC Holdings are set out on page 157.

### All-employee share plans

The exercise period of the options awarded under all-employee share plans may be advanced to an earlier date in certain circumstances, for example on retirement and may be extended in certain circumstances, for example on the death of a participant the executors may exercise the option up to six months beyond the normal exercise period. The closing price per HSBC Holdings ordinary share on 24 April 2007, the day before options were awarded in 2007, was £9.21. The options are exercisable at a 20 per cent discount to the average market value of the ordinary shares on the five business days immediately preceding the invitation date, unless otherwise indicated.

#### HSBC Holdings Savings-Related Share Option Plan

*HSBC Holdings ordinary shares of US\$0.50*

| Date of award | Exercise price (£) | Exercisable from | Exercisable until | Options at 1 January 2007 | Options awarded during period | Options exercised during period <sup>1</sup> | Options lapsed during period | Options at 30 June 2007 |
|---------------|--------------------|------------------|-------------------|---------------------------|-------------------------------|--|------------------------------|-------------------------|
| 11 Apr 2001   | 6.7536             | 1 Aug 2006       | 31 Jan 2007       | 59,421                    |                               | 44,048                                       | 15,124                       | 249                     |
| 2 May 2002    | 6.3224             | 1 Aug 2007       | 31 Jan 2008       | 3,552,436                 |                               | 36,797                                       | 57,905                       | 3,457,734               |
| 23 Apr 2003   | 5.3496             | 1 Aug 2006       | 31 Jan 2007       | 177,912                   |                               | 128,294                                      | 42,809                       | 6,809                   |

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|             |        |            |             |            |        |         |            |
|-------------|--------|------------|-------------|------------|--------|---------|------------|
| 23 Apr 2003 | 5.3496 | 1 Aug 2008 | 31 Jan 2009 | 11,001,155 | 90,864 | 216,276 | 10,694,015 |
| 21 Apr 2004 | 6.4720 | 1 Aug 2007 | 31 Jan 2008 | 3,110,196  | 44,841 | 105,559 | 2,959,796  |
| 21 Apr 2004 | 6.4720 | 1 Aug 2009 | 31 Jan 2010 | 5,295,786  | 23,859 | 169,512 | 5,102,415  |
| 24 May 2005 | 6.6792 | 1 Aug 2008 | 31 Jan 2009 | 3,959,600  | 27,397 | 199,969 | 3,732,234  |
| 24 May 2005 | 6.6792 | 1 Aug 2010 | 31 Jan 2011 | 5,329,930  | 14,854 | 192,010 | 5,123,066  |
| 26 Apr 2006 | 7.6736 | 1 Aug 2009 | 31 Jan 2010 | 4,653,146  | 10,586 | 544,480 | 4,098,080  |
| 26 Apr 2006 | 7.6736 | 1 Aug 2011 | 31 Jan 2012 | 3,550,685  | 2,631  | 341,542 | 3,206,512  |
| 25 Apr 2007 | 7.0872 | 1 Aug 2010 | 31 Jan 2011 | 6,166,897  |        | 32,103  | 6,134,794  |
| 25 Apr 2007 | 7.0872 | 1 Aug 2012 | 31 Jan 2013 | 4,228,735  |        | 18,678  | 4,210,057  |

1 The weighted average closing price of the shares immediately before the dates on which options were exercised was £9.29.

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HSBC HOLDINGS PLC

**Additional Information** (continued)

The fair value of options granted in the period under the Plan was £42 million.

HSBC Holdings Savings-Related Share Option Plan: International  
*HSBC Holdings ordinary shares of US\$0.50*

| Date of award | Exercise price (£) | Exercisable from | Exercisable until | Options at 1 January 2007 | Options awarded during period | Options exercised during period | Options lapsed during period | Options at 30 June 2007 |
|---------------|--------------------|------------------|-------------------|---------------------------|-------------------------------|---------------------------------|------------------------------|-------------------------|
| 11 Apr 2001   | 6.7536             | 1 Aug 2006       | 31 Jan 2007       | 40,853                    |                               | 11,473                          | 9,458                        | 19,922                  |
| 2 May 2002    | 6.3224             | 1 Aug 2007       | 31 Jan 2008       | 1,063,521                 |                               | 4,388                           | 136,262                      | 922,871                 |
| 23 Apr 2003   | 5.3496             | 1 Aug 2008       | 31 Jan 2009       | 10,488                    |                               |                                 |                              | 10,488                  |
| 8 May 2003    | 5.3496             | 1 Aug 2006       | 31 Jan 2007       | 310,378                   |                               | 120,785                         | 104,531                      | 85,062                  |
| 8 May 2003    | 5.3496             | 1 Aug 2008       | 31 Jan 2009       | 5,827,034                 |                               | 56,120                          | 563,306                      | 5,207,608               |
| 21 Apr 2004   | 6.4720             | 1 Aug 2007       | 31 Jan 2008       | 47,070                    |                               |                                 |                              | 47,070                  |
| 21 Apr 2004   | 6.4720             | 1 Aug 2009       | 31 Jan 2010       | 12,365                    |                               |                                 |                              | 12,365                  |
| 10 May 2004   | 6.4720             | 1 Aug 2007       | 31 Jan 2008       | 8,613,295                 |                               | 53,040                          | 732,119                      | 7,828,136               |
| 10 May 2004   | 6.4720             | 1 Aug 2009       | 31 Jan 2010       | 2,953,476                 |                               | 17,328                          | 271,916                      | 2,664,232               |
| 24 May 2005   | 6.6792             | 1 Aug 2008       | 31 Jan 2009       | 10,956,064                |                               | 63,018                          | 865,412                      | 10,027,634              |
| 24 May 2005   | 6.6792             | 1 Aug 2010       | 31 Jan 2011       | 3,743,916                 |                               | 11,318                          | 200,707                      | 3,531,891               |
| 26 Apr 2006   | 7.6736             | 1 Aug 2007       | 31 Oct 2007       | 860,609                   |                               | 822                             | 40,306                       | 819,481                 |
| 26 Apr 2006   | 7.6736             | 1 Aug 2009       | 31 Jan 2010       | 2,324,779                 |                               | 1,359                           | 157,850                      | 2,165,570               |
| 26 Apr 2006   | 7.6736             | 1 Aug 2011       | 31 Jan 2012       | 518,112                   |                               |                                 | 24,419                       | 493,693                 |
| 25 Apr 2007   | 7.0872             | 1 Aug 2008       | 31 Oct 2008       |                           | 1,647,064                     |                                 | 2,161                        | 1,644,903               |
| 25 Apr 2007   | 7.0872             | 1 Aug 2010       | 31 Jan 2011       |                           | 3,573,175                     |                                 | 6,543                        | 3,566,632               |
| 25 Apr 2007   | 7.0872             | 1 Aug 2012       | 31 Jan 2013       |                           | 1,019,913                     |                                 | 3,143                        | 1,016,770               |
|               | (US\$)             |                  |                   |                           |                               |                                 |                              |                         |
| 26 Apr 2006   | 14.16212           | 1 Aug 2007       | 31 Oct 2007       | 591,818                   |                               |                                 | 73,026                       | 518,792                 |
| 26 Apr 2006   | 13.3290            | 1 Aug 2007       | 31 Oct 2007       | 112,660                   |                               | 1,605                           | 6,422                        | 104,633                 |
| 26 Apr 2006   | 13.3290            | 1 Aug 2009       | 31 Jan 2010       | 1,749,146                 |                               | 1,294                           | 144,024                      | 1,603,828               |
| 26 Apr 2006   | 13.3290            | 1 Aug 2011       | 31 Jan 2012       | 478,476                   |                               | 469                             | 50,125                       | 427,882                 |
| 25 Apr 2007   | 14.74782           | 1 Aug 2008       | 31 Oct 2008       |                           | 729,015                       |                                 | 81                           | 728,934                 |
| 25 Apr 2007   | 13.8803            | 1 Aug 2008       | 31 Oct 2008       |                           | 347,176                       |                                 |                              | 347,176                 |
| 25 Apr 2007   | 13.8803            | 1 Aug 2010       | 31 Jan 2011       |                           | 2,817,545                     |                                 | 670                          | 2,816,875               |
| 25 Apr 2007   | 13.8803            | 1 Aug 2012       | 31 Jan 2013       |                           | 804,104                       |                                 |                              | 804,104                 |
|               | ( )                |                  |                   |                           |                               |                                 |                              |                         |
| 26 Apr 2006   | 11.0062            | 1 Aug 2007       | 31 Oct 2007       | 42,046                    |                               |                                 | 1,889                        | 40,157                  |
| 26 Apr 2006   | 11.0062            | 1 Aug 2009       | 31 Jan 2010       | 188,857                   |                               |                                 | 5,133                        | 183,724                 |
| 26 Apr 2006   | 11.0062            | 1 Aug 2011       | 31 Jan 2012       | 39,570                    |                               |                                 | 449                          | 39,121                  |

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|             |         |            |             |  |         |  |         |
|-------------|---------|------------|-------------|--|---------|--|---------|
| 25 Apr 2007 | 10.4217 | 1 Aug 2008 | 31 Oct 2008 |  | 128,427 |  | 128,427 |
| 25 Apr 2007 | 10.4217 | 1 Aug 2010 | 31 Jan 2011 |  | 376,440 |  | 376,440 |
| 25 Apr 2007 | 10.4217 | 1 Aug 2012 | 31 Jan 2013 |  | 128,871 |  | 128,871 |

(HK\$)

|             |          |            |             |           |        |         |           |
|-------------|----------|------------|-------------|-----------|--------|---------|-----------|
| 26 Apr 2006 | 103.4401 | 1 Aug 2007 | 31 Oct 2007 | 1,295,846 | 10,660 | 76,049  | 1,209,137 |
| 26 Apr 2006 | 103.4401 | 1 Aug 2009 | 31 Jan 2010 | 4,255,761 | 10,954 | 145,302 | 4,099,505 |
| 26 Apr 2006 | 103.4401 | 1 Aug 2011 | 31 Jan 2012 | 1,110,391 | 1,077  | 40,362  | 1,068,952 |
| 25 Apr 2007 | 108.4483 | 1 Aug 2008 | 31 Oct 2008 | 2,225,766 |        | 1,436   | 2,224,330 |
| 25 Apr 2007 | 108.4483 | 1 Aug 2010 | 31 Jan 2011 | 4,561,313 |        |         | 4,561,313 |
| 25 Apr 2007 | 108.4483 | 1 Aug 2012 | 31 Jan 2013 | 1,350,798 |        | 440     | 1,350,358 |

1 The weighted average closing price of the shares immediately before the dates on which the options were exercised was £9.22.

2 Exercisable at a 15 per cent discount to the average market value of the ordinary shares on the five business days immediately preceding the invitation date.

The fair value of options granted in the period under the Plan was £22 million.

Fair values of share options awarded under all-employee share option plans in 2007, measured at the date of grant of the option, are calculated using a binomial lattice methodology that is based on the underlying assumptions of the Black-Scholes model.

The expected life of options depends on the behaviour of option holders, which is incorporated into the option model consistent with historic observable data. The fair values calculated are inherently subjective and uncertain due to the assumptions made and the limitations of the model used. The significant weighted average assumptions used to estimate the fair value of the options granted in 2007 were as follows:

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|  | 1-year<br>savings-related<br>share option<br>plan | 3-year<br>savings-related<br>share option<br>plans | 5-year<br>savings-related<br>share option<br>plans |
|--|---|--|--|
| Risk-free interest rate (%) <sup>1</sup> | 4.9   | 4.5  | 4.5  |
| Expected life (years) <sup>2</sup>       | 1   | 3  | 5  |
| Expected volatility (%) <sup>3</sup>     | 17.0  | 17.0   | 17.0   |

1 The risk-free interest rate was determined from the UK gilts zero-coupon yield curve for the HSBC Holdings Savings-Related Share Option Plan. A similar yield curve was used for the HSBC Holdings Savings-Related Share Option Plan: International.

2 Expected life is not a single input parameter but a function of various behavioural assumptions.

3 Expected volatility is estimated by considering historic average HSBC share price volatility and implied volatility for traded options over HSBC shares of similar maturity to those of the employee options.

Expected dividend growth, denominated in US dollars, was determined to be 10 per cent for the first 3 years and 8 per cent thereafter, consistent with consensus analyst forecasts.

### Discretionary share incentive plans

The exercise period of the options awarded under discretionary share incentive plans may be advanced to an earlier date in certain circumstances, for example on retirement, and may be extended in certain circumstances, for example on the death of a participant the executors may exercise the option up to twelve months beyond the normal exercise period.

#### HSBC Holdings Executive Share Option Scheme

HSBC Holdings ordinary shares of  
US\$0.50

| Date of award | Exercise price (£) | Exercisable from | Exercisable until | Options at 1 January 2007 | Options exercised during period <sup>1</sup> | Options lapsed during period | Options at 30 June 2007 |
|---------------|--------------------|------------------|-------------------|---------------------------|--|------------------------------|-------------------------|
| 24 Mar 1997   | 5.0160             | 24 Mar 2000      | 24 Mar 2007       | 188,074                   | 188,053                                      | 21                           |                         |
| 12 Aug 1997   | 7.7984             | 12 Aug 2000      | 12 Aug 2007       | 9,000                     |  |                              | 9,000                   |
| 16 Mar 1998   | 6.2767             | 16 Mar 2001      | 16 Mar 2008       | 678,434                   | 36,954                                       | 30,000                       | 611,480                 |
| 29 Mar 1999   | 6.3754             | 3 Apr 2002       | 29 Mar 2009       | 11,808,970                | 933,186                                      | 85,540                       | 10,790,244              |
| 10 Aug 1999   | 7.4210             | 10 Aug 2002      | 10 Aug 2009       | 100,058                   |  |                              | 100,058                 |
| 31 Aug 1999   | 7.8710             | 31 Aug 2002      | 31 Aug 2009       | 4,000                     |  |                              | 4,000                   |
| 3 Apr 2000    | 7.4600             | 3 Apr 2003       | 3 Apr 2010        | 9,248,569                 | 533,348                                      | 114,228                      | 8,600,993               |

1 The weighted average closing price of the shares immediately before the dates on which options were exercised was £9.19.

The HSBC Holdings Executive Share Option Scheme expired on 26 May 2000. No options have been granted under the Scheme since that date.

#### HSBC Holdings Group Share Option Plan

HSBC Holdings ordinary shares of  
US\$0.50

| Date of award | Exercise price (£) | Exercisable from | Exercisable until | Options at 1 January 2007 | Options exercised during period <sup>1</sup> | Options lapsed during period | Options at 30 June 2007 |
|---------------|--------------------|------------------|-------------------|---------------------------|--|------------------------------|-------------------------|
|---------------|--------------------|------------------|-------------------|---------------------------|--|------------------------------|-------------------------|

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|             |        |             |             |            |           |           |            |
|-------------|--------|-------------|-------------|------------|-----------|-----------|------------|
| 4 Oct 2000  | 9.6420 | 4 Oct 2003  | 4 Oct 2010  | 321,176    |           | 6,970     | 314,206    |
| 23 Apr 2001 | 8.7120 | 23 Apr 2004 | 23 Apr 2011 | 29,400,469 | 859,898   | 755,244   | 27,785,327 |
| 30 Aug 2001 | 8.2280 | 30 Aug 2004 | 30 Aug 2011 | 179,193    | 12,575    | 3,000     | 163,618    |
| 7 May 2002  | 8.4050 | 7 May 2005  | 7 May 2012  | 32,501,697 | 1,370,040 | 695,672   | 30,435,985 |
| 30 Aug 2002 | 7.4550 | 30 Aug 2005 | 30 Aug 2012 | 361,600    | 2,500     | 206,500   | 152,600    |
| 2 May 2003  | 6.9100 | 2 May 2006  | 2 May 2013  | 34,541,586 | 2,677,010 | 1,007,755 | 30,856,821 |
| 29 Aug 2003 | 8.1300 | 29 Aug 2006 | 29 Aug 2013 | 445,894    | 7,910     | 20,860    | 417,124    |
| 3 Nov 2003  | 9.1350 | 3 Nov 2006  | 3 Nov 2013  | 3,255,800  |           | 816,000   | 2,439,800  |
| 30 Apr 2004 | 8.2830 | 30 Apr 2007 | 30 Apr 2014 | 57,927,504 | 68,100    | 3,142,528 | 54,716,876 |
| 27 Aug 2004 | 8.6500 | 27 Aug 2007 | 27 Aug 2014 | 332,470    |           | 16,200    | 316,270    |
| 20 Apr 2005 | 8.3620 | 20 Apr 2008 | 20 Apr 2015 | 7,360,795  |           | 265,500   | 7,095,295  |

1 The weighted average closing price of the shares immediately before the dates on which options were exercised was £9.26.

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**Additional Information** (continued)

The HSBC Holdings Group Share Option Plan expired on 26 May 2005. No options have been granted under the Plan since that date.

## The HSBC Share Plan

*HSBC Holdings ordinary shares of US\$0.50*

| Date of award | Exercise price (£) | Exercisable from | Exercisable until | Options at 1 January 2007 | Options awarded during period | Options exercised during period | Options lapsed during period | Options at 30 June 2007 |
|---------------|--------------------|------------------|-------------------|---------------------------|-------------------------------|---------------------------------|------------------------------|-------------------------|
| 21 Jun 2005   | 8.794              | 21 Jun 2008      | 21 Jun 2009       | 552,526                   |                               |                                 |                              | 552,526                 |
| 30 Sep 2005   | 9.170              | 30 Sep 2008      | 30 Sep 2015       | 74,985                    |                               |                                 |                              | 74,985                  |

**Subsidiary Company Share Plans**

## HSBC France and HSBC Private Bank France

When it was acquired in 2000, HSBC France and its subsidiary company, HSBC Private Bank France, operated employee share option plans under which options could be granted over their respective shares. No further options will be granted under either of these companies' plans. The following are details of options to acquire shares in HSBC France and HSBC Private Bank France.

## HSBC France

*shares of 5*

| Date of award | Exercise price ( ) | Exercisable from | Exercisable until | Options at 1 January 2007 | Options exercised during period <sup>1</sup> | Options lapsed during period | Options at 30 June 2007 <sup>1</sup> |
|---------------|--------------------|------------------|-------------------|---------------------------|--|------------------------------|--------------------------------------|
| 7 May 1997    | 37.05              | 7 Jun 2000       | 7 May 2007        | 66,000                    | 66,000                                       |                              |                                      |
| 29 Apr 1998   | 73.48              | 7 Jun 2000       | 29 Apr 2008       | 192,154                   | 38,500                                       |                              | 153,654                              |
| 7 Apr 1999    | 81.71              | 7 Jun 2000       | 7 Apr 2009        | 383,602                   | 43,700                                       |                              | 339,902                              |
| 12 Apr 2000   | 142.50             | 1 Jan 2002       | 12 Apr 2010       | 646,125                   | 30,250                                       |                              | 615,875                              |

<sup>1</sup> Following exercise of the options, the HSBC France shares will be exchanged for HSBC Holdings ordinary shares in the same ratio as for the acquisition of HSBC France (13 HSBC Holdings ordinary shares for each HSBC France share). At 30 June 2007, The HSBC Holdings Employee Benefit Trust 2001 (No. 1) held 12,996,478 HSBC Holdings ordinary shares which may be exchanged for HSBC France shares arising from the exercise of these options.

## HSBC Private Bank France

*shares of 2*

| Date of award | Exercise price ( ) | Exercisable from | Exercisable until | Options at 1 January 2007 | Options exercised during period <sup>1</sup> | Options lapsed during period | Options at 30 June 2007 <sup>1</sup> |
|---------------|--------------------|------------------|-------------------|---------------------------|--|------------------------------|--------------------------------------|
| 21 Dec 1999   | 10.84              | 21 Dec 2000      | 21 Dec 2009       | 57,130                    | 19,380                                       |                              | 37,750                               |



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|             |       |             |             |         |        |         |
|-------------|-------|-------------|-------------|---------|--------|---------|
| 9 Mar 2000  | 12.44 | 27 Jun 2004 | 31 Dec 2010 | 27,626  |        | 27,626  |
|             |       | 15 May      | 15 May      |         |        |         |
| 15 May 2001 | 20.80 | 2002        | 2011        | 155,025 | 11,250 | 143,775 |
| 1 Oct 2002  | 22.22 | 2 Oct 2005  | 1 Oct 2012  | 163,075 | 13,500 | 149,575 |

1 *Following exercise of the options, the HSBC Private Bank France shares will be exchanged for HSBC Holdings ordinary shares in the ratio of 1.83 HSBC Holdings ordinary shares for each HSBC Private Bank France share. At 30 June 2007, The CCF Employee Benefit Trust 2001 held 1,004,568 HSBC Holdings ordinary shares which may be exchanged for HSBC Private Bank France shares arising from the exercise of these options.*

**HSBC Finance and its subsidiaries**

Following the acquisition of HSBC Finance in 2003, all outstanding options and equity-based awards over HSBC Finance common shares were converted into rights to receive HSBC Holdings ordinary shares in the same ratio as the share exchange offer for the acquisition of HSBC Finance (2.675 HSBC Holdings ordinary shares for each HSBC Finance common share) and the exercise prices per share were adjusted accordingly. No further options will be granted under any of these plans.

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All outstanding options and other equity-based awards over HSBC Finance common shares granted before 14 November 2002, being the date the transaction was announced, vested on completion of the acquisition. Options and equity-based awards granted on or after 14 November 2002 are exercisable on their original terms, save that they have been adjusted to reflect the exchange ratio.

At 30 June 2007, the HSBC (Household) Employee Benefit Trust 2003 and the HSBC (Household) Employee Benefit Trust 2003 (No.2) held 9,094,666 HSBC Holdings ordinary shares and 196,752 American Depositary Shares, each of which represents five HSBC Holdings ordinary shares, which may be used to satisfy the exercise of employee share options.

HSBC Finance

### 1996 Long-Term Executive Incentive Compensation Plan

*HSBC Holdings ordinary shares of US\$0.50*

| Date of award | Exercise price (US\$) | Exercisable from | Exercisable until | Options at 1 January 2007 | Options exercised during period <sup>1</sup> | Options lapsed during period | Options at 30 June 2007 |
|---------------|-----------------------|------------------|-------------------|---------------------------|--|------------------------------|-------------------------|
| 14 May 1997   | 11.29                 | 14 May 1998      | 14 May 2007       | 100,315                   |  | 100,315                      |                         |
| 10 Nov 1997   | 14.60                 | 10 Nov 1998      | 10 Nov 2007       | 573,684                   | 193,623                                      | 20,063                       | 359,998                 |
| 15 Jun 1998   | 17.08                 | 15 Jun 1999      | 15 Jun 2008       | 802,500                   | 802,500                                      |                              |                         |
| 1 Jul 1998    | 19.21                 | 1 Jul 1999       | 1 Jul 2008        | 80,250                    |  |                              | 80,250                  |
| 9 Nov 1998    | 13.71                 | 9 Nov 1999       | 9 Nov 2008        | 2,015,391                 | 614,958                                      |                              | 1,400,433               |
| 17 May 1999   | 16.99                 | 17 May 2000      | 17 May 2009       | 334,375                   |  |                              | 334,375                 |
| 31 Aug 1999   | 13.96                 | 31 Aug 2000      | 31 Aug 2009       | 331,701                   | 13,375                                       |                              | 318,326                 |
| 8 Nov 1999    | 16.96                 | 8 Nov 2000       | 8 Nov 2009        | 4,729,402                 | 331,700                                      |                              | 4,397,702               |
| 30 Jun 2000   | 15.70                 | 30 Jun 2001      | 30 Jun 2010       | 26,846                    |  |                              | 26,846                  |
| 8 Feb 2000    | 13.26                 | 8 Feb 2001       | 8 Feb 2010        | 66,875                    |  |                              | 66,875                  |
| 13 Nov 2000   | 18.40                 | 13 Nov 2001      | 13 Nov 2010       | 6,295,614                 |  |                              | 6,295,614               |
| 12 Nov 2001   | 21.37                 | 12 Nov 2002      | 12 Nov 2011       | 7,514,344                 |  |                              | 7,514,344               |
| 20 Nov 2002   | 10.66                 | 20 Nov 2003      | 20 Nov 2012       | 3,125,202                 | 601,875                                      |                              | 2,523,327               |

<sup>1</sup> The weighted average closing price of the shares immediately before the dates on which options were exercised was £9.36.

<sup>2</sup> 25 per cent of the original award is exercisable on each of the first, second, third and fourth anniversaries of the date of award. The exercise period may be advanced to an earlier date in certain circumstances, e.g. retirement.

HSBC Finance

### 1996 Long-Term Executive Incentive Compensation Plan<sup>1</sup>

*HSBC Holdings ordinary shares of US\$0.50*

| Date of award | Vesting from <sup>2</sup> | Vesting until <sup>2</sup> | Rights at 1 January 2007 | Rights vested during period <sup>3</sup> | Rights lapsed during period | Rights at 30 June 2007 |
|---------------|---------------------------|----------------------------|--------------------------|--|-----------------------------|------------------------|
| 15 Nov 2002   | 15 Nov 2005               | 15 Nov 2007                | 2,409                    |  |                             | 2,409                  |
| 20 Nov 2002   | 20 Nov 2005               | 20 Nov 2007                | 539,027                  | 18,094                                   | 11,697                      | 509,236                |

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|             |            |            |        |        |        |
|-------------|------------|------------|--------|--------|--------|
| 2 Dec 2002  | 2 Dec 2005 | 2 Dec 2007 | 3,123  |        | 3,123  |
|             | 16 Dec     | 16 Dec     |        |        |        |
| 16 Dec 2002 | 2005       | 2007       | 11,774 |        | 11,774 |
|             | 20 Dec     | 20 Dec     |        |        |        |
| 20 Dec 2002 | 2005       | 2007       | 88,286 | 44,136 | 44,150 |
| 2 Jan 2003  | 2 Jan 2006 | 2 Jan 2008 | 893    | 446    | 447    |
|             | 15 Jan     | 15 Jan     |        |        |        |
| 15 Jan 2003 | 2006       | 2008       | 20,959 | 10,479 | 10,480 |
| 3 Feb 2003  | 3 Feb 2006 | 3 Feb 2008 | 6,344  | 3,170  | 3,174  |
|             | 14 Feb     | 14 Feb     |        |        |        |
| 14 Feb 2003 | 2006       | 2008       | 98,265 | 49,131 | 49,134 |
|             | 3 Mar      | 3 Mar      |        |        |        |
| 3 Mar 2003  | 2006       | 2008       | 893    | 446    | 447    |

- 1 *Awards of Restricted Stock Rights which represent a right to receive shares for nil consideration if the employee remains in the employment of HSBC Finance at the date of vesting.*
- 2 *Restricted Stock Rights vest one-third on each of the third, fourth and fifth anniversaries of the date of award. May be advanced to an earlier date in certain circumstances, e.g. retirement.*
- 3 *The weighted average closing price of the shares immediately before the dates on which rights vested was £9.20.*

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HSBC HOLDINGS PLC

**Additional Information** (continued)

Beneficial Corporation

**1990 Non-Qualified Stock Option Plan***HSBC Holdings ordinary shares of US\$0.50*

| Date of award | Exercise price (US\$) | Exercisable from | Exercisable until | Options at 1 January 2007 | Options exercised during period <sup>1</sup> | Options lapsed during period | Options at 30 June 2007 |
|---------------|-----------------------|------------------|-------------------|---------------------------|--|------------------------------|-------------------------|
| 14 Nov 1997   | 9.20                  | 14 Nov 1998      | 14 Nov 2007       | 131,248                   |  | 65,624                       | 65,624                  |
| 19 Nov 1997   | 9.39                  | 19 Nov 1998      | 19 Nov 2007       | 309,225                   | 170,590                                      |                              | 138,635                 |
| 1 Dec 1997    | 9.68                  | 1 Dec 1998       | 1 Dec 2007        | 49,218                    |  | 16,406                       | 32,812                  |

<sup>1</sup> The weighted average closing price of the shares immediately before the dates on which options were exercised was £9.34.

Beneficial Corporation

**BenShares Equity Participation Plan***HSBC Holdings ordinary shares of US\$0.50*

| Date of award | Exercise price (US\$) | Exercisable from | Exercisable until | Options at 1 January 2007 | Options exercised during period <sup>1</sup> | Options lapsed during period | Options at 30 June 2007 |
|---------------|-----------------------|------------------|-------------------|---------------------------|--|------------------------------|-------------------------|
| 31 Jan 1997   | 9.87                  | 31 Jan 1998      | 31 Jan 2007       | 20,113                    | 10,261                                       | 9,852                        |                         |
| 15 Nov 1997   | 11.04                 | 15 Nov 1998      | 15 Nov 2007       | 35,586                    | 4,105  |                              | 31,481                  |

<sup>1</sup> The weighted average closing price of the shares immediately before the dates on which options were exercised was £9.35.

Renaissance Holdings, Inc.

**Amended and Restated 1997 Stock Incentive Plan***HSBC Holdings ordinary shares of US\$0.50*

| Date of award | Exercise price (US\$) | Exercisable from | Exercisable until | Options at 1 January 2007 | Options exercised during period | Options lapsed during period | Options at 30 June 2007 |
|---------------|-----------------------|------------------|-------------------|---------------------------|---------------------------------|------------------------------|-------------------------|
| 31 Oct 1997   | 1.25                  | 31 Oct 1998      | 31 Oct 2007       | 1,325                     |                                 |                              | 1,325                   |
| 1 Jan 1998    | 1.25                  | 1 Jan 1999       | 1 Jan 2008        | 1,424                     |                                 |                              | 1,424                   |

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|            |      |            |            |       |       |
|------------|------|------------|------------|-------|-------|
| 1 Oct 1998 | 1.74 | 1 Oct 1999 | 1 Oct 2008 | 803   | 803   |
| 1 Jan 1999 | 2.24 | 1 Jan 2000 | 1 Jan 2009 | 5,024 | 5,024 |

### **Bank of Bermuda**

Following the acquisition of The Bank of Bermuda Limited ( Bank of Bermuda ) in 2004, all outstanding options over Bank of Bermuda shares were converted into rights to receive HSBC Holdings ordinary shares based on the consideration of US\$40 for each Bank of Bermuda share and the average closing price of HSBC Holdings ordinary shares, derived from the London Stock Exchange Daily Official List, for the five business days preceding the closing date of the acquisition. No further options will be granted under any of these plans.

All outstanding options over Bank of Bermuda shares vested on completion of the acquisition. At 30 June 2007, the HSBC (Bank of Bermuda) Employee Benefit Trust 2004 held 1,949,092 HSBC Holdings ordinary shares which may be used to satisfy the exercise of these options.

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Bank of Bermuda

**Executive Share Option Plan 1997***HSBC Holdings ordinary shares of US\$0.50*

| Date of award | Exercise price (US\$) | Exercisable from | Exercisable until | Options at 1 January 2007 | Options exercised during period <sup>1</sup> | Options lapsed during period | Options at 30 June 2007 |
|---------------|-----------------------|------------------|-------------------|---------------------------|--|------------------------------|-------------------------|
| 1 Jul 1998    | 9.61                  | 1 Jul 1999       | 1 Jul 2008        | 67,813                    |  |                              | 67,813                  |
| 23 Feb 1999   | 7.40                  | 23 Feb 2000      | 23 Feb 2009       | 11,684                    | 6,780  |                              | 4,904                   |
| 3 Aug 1999    | 7.10                  | 3 Aug 2000       | 3 Aug 2009        | 9,331                     | 1,697  |                              | 7,634                   |
| 4 Feb 2000    | 7.21                  | 4 Feb 2001       | 4 Feb 2010        | 40,185                    | 1,540  |                              | 38,645                  |
| 1 Jun 2000    | 7.04                  | 1 Jun 2001       | 1 Jun 2010        | 61,649                    |  |                              | 61,649                  |
| 31 Jul 2000   | 10.11                 | 31 Jul 2001      | 31 Jul 2010       | 27,744                    |  |                              | 27,744                  |
| 11 Jan 2001   | 14.27                 | 11 Jan 2002      | 11 Jan 2011       | 161,829                   | 107,886                                      |                              | 53,943                  |

<sup>1</sup> The weighted average closing price of the shares immediately before the dates on which options were exercised was £8.92.

Bank of Bermuda

**Share Option Plan 2000***HSBC Holdings ordinary shares of US\$0.50*

| Date of award | Exercise price (US\$) | Exercisable from | Exercisable until | Options at 1 January 2007 | Options exercised during period <sup>1</sup> | Options lapsed during period | Options at 30 June 2007 |
|---------------|-----------------------|------------------|-------------------|---------------------------|--|------------------------------|-------------------------|
| 11 Jan 2001   | 14.27                 | 11 Jan 2002      | 11 Jan 2011       | 134,857                   |  |                              | 134,857                 |
| 6 Feb 2001    | 16.41                 | 6 Feb 2002       | 6 Feb 2011        | 630,646                   | 36,482                                       |                              | 594,164                 |
| 29 Mar 2001   | 15.39                 | 29 Mar 2002      | 29 Mar 2011       | 270                       |  |                              | 270                     |
| 16 Apr 2001   | 15.57                 | 16 Apr 2002      | 16 Apr 2011       | 539                       |  |                              | 539                     |
| 6 Jun 2001    | 18.35                 | 6 Jun 2002       | 6 Jun 2011        | 8,091                     |  |                              | 8,091                   |
| 16 Jul 2001   | 16.87                 | 16 Jul 2002      | 16 Jul 2011       | 14,930                    |  |                              | 14,930                  |
| 28 Aug 2001   | 15.39                 | 28 Aug 2002      | 28 Aug 2011       | 13,486                    |  |                              | 13,486                  |
| 26 Sep 2001   | 12.79                 | 26 Sep 2002      | 26 Sep 2011       | 438,585                   | 81,727                                       |                              | 356,858                 |
| 30 Jan 2002   | 15.60                 | 30 Jan 2003      | 30 Jan 2012       | 1,226                     |  |                              | 1,226                   |
| 5 Feb 2002    | 16.09                 | 5 Feb 2003       | 5 Feb 2012        | 865,382                   | 61,122                                       |                              | 804,260                 |
| 10 Jul 2002   | 15.84                 | 10 Jul 2003      | 10 Jul 2012       | 12,260                    |  |                              | 12,260                  |
| 4 Feb 2003    | 10.69                 | 4 Feb 2004       | 4 Feb 2013        | 139,658                   | 6,616  |                              | 133,042                 |
| 21 Apr 2003   | 11.85                 | 21 Apr 2004      | 21 Apr 2013       | 20,840                    | 14,007                                       |                              | 6,833                   |

<sup>1</sup> The weighted average closing price of the shares immediately before the dates on which options were exercised was £9.05.

Bank of Bermuda

**Directors Share Option Plan***HSBC Holdings ordinary shares of US\$0.50*

| Date of award | Exercise price (US\$) | Exercisable from | Exercisable until | Options at 1 January | Options exercised during | Options lapsed during | Options at 30 June |
|---------------|-----------------------|------------------|-------------------|----------------------|--------------------------|-----------------------|--------------------|
|---------------|-----------------------|------------------|-------------------|----------------------|--------------------------|-----------------------|--------------------|

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| award       | price (US\$) | from        | until       | 2007   | period | period | 2007   |
|-------------|--------------|-------------|-------------|--------|--------|--------|--------|
| 22 Sep 1999 | 8.02         | 22 Sep 2000 | 22 Sep 2009 | 3,082  |        |        | 3,082  |
| 20 Sep 2000 | 11.31        | 20 Sep 2001 | 20 Sep 2010 | 4,046  |        |        | 4,046  |
| 28 Mar 2001 | 15.76        | 28 Mar 2002 | 28 Mar 2011 | 12,811 |        |        | 12,811 |
| 3 Apr 2002  | 16.01        | 3 Apr 2003  | 3 Apr 2012  | 24,520 |        |        | 24,520 |
| 30 Apr 2003 | 12.23        | 30 Apr 2004 | 30 Apr 2013 | 4,904  |        |        | 4,904  |

### 3 Notifiable interests in share capital

---

The following notifications have been received pursuant to the Financial Services Authority's Disclosure and Transparency Rule 5:

- Legal and General Group plc gave notice on 11 May 2007 that it had a holding on 10 May 2007 of 463,596,251 HSBC Holdings ordinary shares, representing 3.96 per cent of the ordinary shares in issue at that date;
- Deutsche Bank AG gave notice on 27 March 2007 that it had a holding on 23 March 2007 of 376,121,314 HSBC Holdings ordinary shares, representing 3.25 per cent of the ordinary shares in issue at that date;

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HSBC HOLDINGS PLC

## Additional Information (continued)

- Singularis Holdings Limited, AWAL Trust Company Limited and Maan Abdulwahed Al-Sanea gave notice on 16 April 2007 that they had a holding on 16 April 2007 of 360,055,575 HSBC Holdings ordinary shares, representing 3.11 per cent of the ordinary shares in issue at that date; and
- Barclays plc gave notice on 17 April 2007 that it had a holding on 16 April 2007 of 518,233,657 HSBC Holdings ordinary shares, representing 4.47 per cent of the ordinary shares in issue at that date.

There are no notifiable interests in the equity share capital recorded in the register maintained under section 336 of the Securities and Futures Ordinance of Hong Kong.

### 4 Dealings in HSBC Holdings shares

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Except for dealings as intermediaries by HSBC Bank, HSBC Financial Products (France) and The Hongkong and Shanghai Banking Corporation, which are members of a European Economic Area exchange, neither HSBC Holdings nor any subsidiary undertaking has bought, sold or redeemed any securities of HSBC Holdings during the six months ended 30 June 2007.

### 5 Second interim dividend for 2007

---

The Directors have declared a second interim dividend for 2007 of US\$0.17 per ordinary share. The second interim dividend will be payable on 4 October 2007 to holders of ordinary shares on the Register at the close of business on 17 August 2007. The dividend will be payable in cash, in US dollars, sterling or Hong Kong dollars, or a combination of these currencies, at the exchange rates quoted by HSBC Bank plc in London at or about 11.00 am on 24 September 2007, and with a scrip dividend alternative. Particulars of these arrangements will be mailed to shareholders on or about 29 August 2007, and elections must be received by 19 September 2007.

The dividend will be payable on shares held through Euroclear France, the settlement and central depository system for Euronext Paris, on 4 October 2007 to the holders of record on 17 August 2007. The dividend will be payable in cash in euros at the exchange rate on 24 September 2007, or as a scrip dividend. Particulars of these arrangements will be announced through Euronext Paris on 15 August and 22 August 2007.

The dividend will be payable on American Depositary Shares ( ADSs ), each of which represents five ordinary shares, on 4 October 2007 to holders of record on 17 August 2007. The dividend of US\$0.85 per ADS will be payable in cash in US dollars or as a scrip dividend of new ADSs. Particulars of these arrangements will be mailed to holders on or about 24 August 2007. Elections must be received by the depository on or before 14 September 2007. Alternatively, the cash dividend may be invested in additional ADSs for participants in the dividend reinvestment plan operated by the depository.

HSBC Holdings ordinary shares will be quoted ex-dividend in London, Hong Kong and Bermuda on 15 August 2007 and in Paris on 20 August 2007. The ADSs will be quoted ex-dividend in New York on 15 August 2007.

The Overseas Branch Register of shareholders in Hong Kong will be closed for one day, on Friday 17 August 2007. Any person who has acquired shares registered on the Hong Kong Branch Register but who has not lodged the share transfer with the Hong Kong Branch Registrar should do so before 4.00 pm on Thursday 16 August 2007 in order to receive the second interim dividend for 2007, which will be payable on 4 October 2007. Transfers may not be made to or from the Hong Kong Overseas Branch Register while that Branch Register is closed.

Any person who has acquired shares registered on the Principal Register in the United Kingdom but who has not lodged the share transfer with the Principal Registrar should do so before 4.00 pm on Friday 17 August 2007 in order to receive the dividend.

Any person who has acquired shares registered on the Overseas Branch Register of shareholders in Bermuda but who has not lodged the share transfer with the Bermuda Branch Registrar should do so before 4.00 pm on Friday 17 August 2007 in order to receive the dividend.



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Transfers of American Depositary Shares must be lodged with the depositary by 12 noon on Friday 17 August 2007 in order to receive the dividend.

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[Back to Contents](#)**6 Proposed third interim dividend for 2007**

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The Board has adopted a policy of paying quarterly dividends on the ordinary shares. Under this policy it is intended to have a pattern of three equal interim dividends with a variable fourth interim dividend. It is envisaged that the third interim dividend for 2007 will be US\$0.17 per ordinary share. The proposed timetable for the third interim dividend for 2007 payable on the ordinary shares is:

|   |                     |
|---|---------------------|
| Announcement  | 5 November<br>2007  |
| American Depositary Shares quoted ex-dividend in New York                                 | 20 November<br>2007 |
| Shares quoted ex-dividend in London, Hong Kong and Bermuda                                | 21 November<br>2007 |
| Record date and closure of Hong Kong Overseas Branch Register of shareholders for one day | 23 November<br>2007 |
| Shares quoted ex-dividend in Paris  | 26 November<br>2007 |
| Payment date  | 16 January 2008     |

**7 Final results and fourth interim dividend for 2007**

---

The results for the year to 31 December 2007 will be announced on Monday 3 March 2008. It is intended that any fourth interim dividend for 2007 that is announced on that date would be payable on 7 May 2008 to shareholders on the Register on 25 March 2008. HSBC Holdings ordinary shares would be quoted ex-dividend in London, Hong Kong and Bermuda on 19 March 2008 and in Paris on 26 March 2008. The American Depositary Shares would be quoted ex-dividend in New York on 20 March 2008.

**8 Corporate governance**

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HSBC is committed to high standards of corporate governance.

HSBC Holdings has complied with the applicable code provisions of the Combined Code on Corporate Governance issued by the Financial Reporting Council throughout the six months to 30 June 2007.

HSBC Holdings has complied with the applicable code provisions of the Code on Corporate Governance Practices in Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited throughout the six months to 30 June 2007.

The Board of HSBC Holdings has adopted a code of conduct for transactions in HSBC Group securities by Directors that complies with The Model Code in the Listing Rules of the Financial Services Authority and with The Model Code for Securities Transactions by Directors of Listed Issuers ( Hong Kong Model Code ) set out in the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, save that The Stock Exchange of Hong Kong Limited has granted certain waivers from strict compliance with the Hong Kong Model Code, primarily to take into account accepted practices in the UK, particularly in respect of employee share plans. Following a specific enquiry, each Director has confirmed he or she has complied with the code of conduct for transactions in HSBC Group securities throughout the period.

There have been no material changes to the information disclosed in the *Annual Report and Accounts 2006* in respect of the number and remuneration of employees, remuneration policies and share option plans.

**9 Telephone and online share dealing service**

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For shareholders on the Principal Register who are resident in the UK, Channel Islands or Isle of Man with a UK, Channel Islands or Isle of Man postal address, and who hold an HSBC Bank personal

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current account, the HSBC InvestDirect sharedealing service is available for buying and selling HSBC Holdings ordinary shares. Details are available from: HSBC InvestDirect, Exchange Place, Poseidon Way, Leamington Spa, Warwickshire CV34 6BY, UK, telephone: 08456 002 469, web: [www.hsbc.co.uk/shares](http://www.hsbc.co.uk/shares).

### 10 Stock codes

---

HSBC Holdings plc ordinary shares trade under the following stock codes:

|                               |      |
|-------------------------------|------|
| London Stock Exchange         | HSBA |
| Hong Kong Stock Exchange      | 5    |
| New York Stock Exchange (ADS) | HBC  |
| Euronext Paris                | HSB  |
| Bermuda Stock Exchange        | HSBC |

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HSBC HOLDINGS PLC

**Additional Information** (continued)

**11 Copies of the *Interim Report 2007***

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Further copies of the *Interim Report 2007* may be obtained from Group Communications, HSBC Holdings plc, 8 Canada Square, London E14 5HQ, United Kingdom; or from Group Public Affairs, The Hongkong and Shanghai Banking Corporation Limited, 1 Queen's Road Central, Hong Kong; or from Employee Communications, HSBC-North America, 2700 Sanders Road, Prospect Heights, Illinois 60070, USA; or from the HSBC website, [www.hsbc.com](http://www.hsbc.com).

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A Chinese translation of this and future documents may be obtained on request from the Registrars. Please also contact the Registrars if you have received a Chinese translation of this document and do not wish to receive such translations in the future.

*Principal Register*

Computershare Investor Services PLC  
PO Box 1064  
The Pavilions  
Bridgwater Road  
Bristol BS99 3FA  
United Kingdom

*Hong Kong Overseas Branch Register*

Computershare Hong Kong Investor Services Limited  
Hopewell Centre,  
Rooms 1806-1807, 18<sup>th</sup> Floor  
183 Queen's Road East  
Wan Chai  
Hong Kong

*Bermuda Overseas Branch Register*

Corporate Shareholder Services  
The Bank of Bermuda Limited  
6 Front Street  
Hamilton HM 11  
Bermuda

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HSBC HOLDINGS PLC

**Glossary of Terms**

| <b>Terms used</b>      | <b>Brief description</b>   |
|------------------------|--|
| ADS                    | American depositary share  |
| AIEA                   | Average interest-earning assets  |
| ALCO                   | Asset and liability management committee   |
| ARMs                   | Adjustable rate mortgages  |
| ATM                    | Automated teller machine   |
| Banca Nazionale        | Banca Nazionale del Lavoro SpA   |
| Bank of Bermuda        | The Bank of Bermuda Limited  |
| Bank of Communications | Bank of Communications Limited, mainland China's sixth largest bank, owned 18.6 per cent by HSBC                               |
| Basel I                | The 1988 Basel Capital Accord  |
| Basel II               | Final Accord of the Basel Committee on proposals for a new capital adequacy framework  |
| BIPRU                  | The Prudential Sourcebook for Banks, Building Societies and Investment Firms, published by the FSA                             |
| CIBM                   | Corporate, Investment Banking and Markets  |
| CPI                    | Consumer Price Index   |
| CRD                    | EU Capital Requirements Directive  |
| Cyprus Popular Bank    | The Cyprus Popular Bank Limited  |
| DPF                    | Discretionary participation features   |
| Erisa                  | Together, Erisa S.A., the French life insurer, and Erisa I.A.R.D, the property and casualty insurer                            |
| EU                     | European Union   |
| FSA                    | Financial Services Authority (UK)  |
| FTSE                   | Financial Times-Stock Exchange index   |
| GAAP                   | Generally accepted accounting principles   |
| GDP                    | Gross domestic product   |
| GENPRU                 | The General Prudential Sourcebook, published by the FSA  |
| Global Markets         | HSBC's treasury and capital markets services in Corporate, Investment Banking and Markets                                      |
| Group                  | HSBC Holdings together with its subsidiary undertakings  |
| Grupo Banistmo         | Grupo Banistmo S.A., the leading banking group in Central America, which was acquired in November 2006.                        |
| Hong Kong              | Hong Kong Special Administrative Region of the People's Republic of China  |
| HSBC                   | HSBC Holdings together with its subsidiary undertakings  |
| HSBC Bank              | HSBC Bank plc, formerly Midland Bank plc   |
| HSBC Direct            | HSBC's online banking and savings proposition  |
| HSBC Finance           | HSBC Finance Corporation, the US consumer finance company acquired in 2003 (formerly Household International, Inc.)            |
| HSBC France            | HSBC's French banking subsidiary (formerly CCF S.A.)   |
| HSBC Holdings          | HSBC Holdings plc  |
| HSBC Premier           | HSBC's premium global banking service  |
| IAS                    | International Accounting Standard  |
| IASB                   | International Accounting Standards Board   |
| IFRIC                  | International Financial Reporting Interpretations Committee  |
| IFRSs                  | International Financial Reporting Standards  |
| Industrial Bank        | Industrial Bank Co. Limited, a national joint-stock bank in mainland China of which Hang Seng Bank Limited owns 12.78 per cent |
| IPO                    | Initial public offering  |
| IRB                    | Internal ratings based approach to implementing Basel II   |
| IVAs                   | Individual voluntary arrangements (UK)   |
| Mainland China         | People's Republic of China excluding Hong Kong   |
| M&S                    | Marks and Spencer  |
| MSCI                   | Morgan Stanley Capital International index   |
| OFT                    | Office of Fair Trading (UK)  |



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HSBC HOLDINGS PLC

**Glossary of Terms** (continued)

| <b>Terms used</b> | <b>Brief description</b>                                       |
|-------------------|--|
| Option ARMs       | Adjustable-rate mortgages with alternative payment options     |
| Ping An Insurance | Ping An Insurance (Group) Company of China, Limited            |
| Seasoning         | The emergence of loss patterns in a credit portfolio over time |
| SEC               | Securities and Exchange Commission (US)                        |
| TSR               | Total shareholder return                                       |
| UK                | United Kingdom   |
| US                | United States of America                                       |
| US GAAP           | US Generally Accepted Accounting Principles                    |
| VAR               | Value at risk  |

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This document comprises the *Interim Report 2007* to shareholders and information contained herein is being filed on Form 6-K with the US Securities and Exchange Commission ( SEC ), for HSBC Holdings plc and its subsidiary and associated undertakings.

**HSBC HOLDINGS PLC**

*Incorporated in England with limited liability. Registered in England: number 617987*

**REGISTERED OFFICE AND GROUP HEAD OFFICE**

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SIGNATURE

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorised.

HSBC Holdings plc

By: /s/ D J FLINT

Name: D J Flint

Title: Group Finance Director

3 August 2007

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