HSBC HOLDINGS PLC
Form 6-K
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SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

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, 2008

HSBC Holdings plc

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

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 30, 2008, other than pages 149, 237 and 238 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, 333-135007, 333-143639 and 333-145859.

H S B C H O L D I N G S P L C

Interim Report 2008

Headquartered in London, HSBC is one of the largest banking and financial services organisations in the world. Its international network comprises some 11,000 properties in 85 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 100 million customers through four customer groups and global businesses: Personal Financial Services (including consumer finance); Commercial Banking; Global Banking and Markets; and Private Banking.

Certain defined terms

Unless the context requires otherwise, HSBC Holdings means HSBC Holdings plc and HSBC or the Group 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 ordin shares and those preference shares classified as equity.

The Interim Report 2008 *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 207 to 236, have been prepared in accordance with International Accounting Standard (IAS) 34 Interim Financial Reporting as issued by the International Accounting Standards Board (IASB) and endorsed by the European Union (EU). The consolidated financial statements of HSBC at 31 December 2007 were prepared in accordance with International Financial Reporting Standards (IFRSs) as issued by the IASB, and as endorsed by the EU. EU-endorsed IFRSs may differ from IFRSs as published by the IASB if, at any point in time, new or amended IFRSs have not been endorsed by the EU. At 30 June 2008, there were no unendorsed standards effective for the period ended 30 June 2008 affecting these consolidated financial statements, and there was no difference between IFRSs endorsed by the EU and IFRSs issued by the IASB in terms of their application to 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, the information presented in this document has been prepared in accordance with IFRSs.

When reference is made to underlying or underlying basis in tables or commentaries, comparative information has been expressed at constant currency (see page 4) and adjusted for the effects of acquisitions and disposals.

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1 *Detailed contents are provided on the referenced page.*

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H S B C H O L D I N G S P L C

Financial Highlights

For the half-year

- Net operating income before loan impairment charges up by US$982 million, 3 per cent, to US$39,475 million (US$38,493 million in the first half of 2007).
- Loan impairment charges and other credit risk provisions up by US$3,712 million (58 per cent) to US$10,058 million (US$6,346 million in the first half of 2007).
- Group pre-tax profit down by US$3,912 million (28 per cent) to US$10,247 million (US$14,159 million in the first half of 2007).
- Profit attributable to shareholders of the parent company down by US$3,173 million, 29 per cent, to US$7,722 million (US$10,895 million in the first half of 2007).
- Return on average shareholders equity of 12.1 per cent (19.1 per cent in the first half of 2007).
- Earnings per share down 32 per cent to US$0.65 (US$0.95 in the first half of 2007).

Dividends and capital position

- Second interim dividend for 2008 of US$0.18 per share which, together with the first interim dividend for 2008 of US$0.18 per share already paid, represents an increase of 6 per cent over the first and second interim dividends for 2007.
- Tier 1 capital ratio of 8.8 per cent and total capital ratio of 11.9 per cent.

Cautionary statement regarding forward-looking statements

This *Interim Report 2008* 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 the *Annual Report and Accounts 2007*.

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Profitability and balance sheet data

	Half-year to		
	30 June 2008 US$m	30 June 2007 US$m	31 December 2007 US$m
For the period			
Total operating income	**42,912**	42,092	45,509
Profit before tax	**10,247**	14,159	10,053
Profit attributable to shareholders of the parent company	**7,722**	10,895	8,238
Dividends	**6,823**	6,192	4,049
At the period-end			
Total equity	**134,011**	126,491	135,416
Total shareholders equity	**126,785**	119,780	128,160
Capital resources[1,2]	**146,950**	137,042	152,640
Customer accounts	**1,161,923**	980,832	1,096,140
Total assets	**2,546,678**	2,150,441	2,354,266
Risk-weighted assets[2]	**1,231,481**	1,041,540	1,123,782
	US$	US$	US$
Per ordinary share			
Basic earnings	**0.65**	0.95	0.70
Diluted earnings	**0.65**	0.94	0.69
Dividends	**0.57**	0.53	0.34
Net asset value at period end	**10.27**	10.10	10.72

Capital and performance ratios (annualised)

	%	%	%
Capital ratios[2]			
Tier 1 capital	**8.8**	9.3	9.3
Total capital	**11.9**	13.2	13.6
Performance ratios			
Return on average invested capital[3]	**11.9**	18.4	12.4
Return on average total shareholders equity[4]	**12.1**	19.1	13.0
Post-tax return on average total assets	**0.68**	1.19	0.78
Post-tax return on average risk-weighted assets	**1.39**	2.30	1.63
Credit coverage ratios			
Loan impairment charges as a percentage of total operating income	**23.2**	15.0	23.8
Loan impairment charges as a percentage of average gross customer advances	**2.04**	1.53	2.48
Total impairment allowances outstanding as a percentage of impaired loans at period end	**108.1**	98.4	104.9
Efficiency and revenue mix ratios			
Cost efficiency ratio[5]	**51.0**	48.3	50.4
As a percentage of total operating income:			
net interest income	**49.4**	43.3	43.0
net fee income	**25.6**	24.9	25.3
net trading income	**8.9**	13.1	9.5
Financial ratio			
Average total shareholders equity to average total assets	**5.2**	5.9	5.5

1 *Capital resources are total regulatory capital, the calculation of which is set out on page 201.*
2 *The calculation of capital resources, capital ratios and risk-weighted assets for 30 June 2008 is on a Basel II basis. Comparatives are based on Basel I.*
3 *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 111.*
4 *The return on average total shareholders equity is defined as profit attributable to shareholders of the parent company divided by average total shareholders equity.*
5 *The cost efficiency ratio is defined as total operating expenses divided by net operating income before loan impairment charges and other credit risk provisions.*

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Financial Highlights (continued)

Share information

	At 30 June 2008	At 30 June 2007	At 31 December 2007
US$0.50 ordinary shares in issue (million)	**12,005**	11,713	11,829
Market capitalisation (billion)	**US$185**	US$215	US$198
Closing market price per ordinary share:			
London	**£7.76**	£9.15	£8.42
Hong Kong	**HK$120.90**	HK$142.50	HK$131.70
Closing market price per American Depositary Share (ADS[1])	**US$76.70**	US$91.77	US$83.71

	Over 1 year	**Over 3 years**	**Over 5 years**
HSBC total shareholder return to 30 June 2008[2]	**90.1**	**102.3**	**141.0**
Benchmarks:			
FTSE 100[3]	88.4	122.2	166.0
MSCI World[4]	89.8	131.1	180.6

1 *Each ADS represents five ordinary shares.*
2 *Total shareholder return is defined on page 12 of the* Annual Report and Accounts 2007.
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 2007 and 31 December 2007, used in the 2008 commentaries, are computed by retranslating into US dollars:

- the income statements for the half-years to 30 June 2007 and 31 December 2007 of non-US dollar branches, subsidiaries, joint ventures and associates at the average rates of exchange for the half-year to 30 June 2008; and
- the balance sheets at 30 June 2007 and 31 December 2007 for non-US dollar branches, subsidiaries, joint ventures and associates at the rates of exchange ruling at 30 June 2008.

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.

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Group Chairman s Statement

The first half of 2008 saw the most difficult financial markets for several decades, marked by significant declines in profitability throughout much of our industry, with consequent recapitalisation and restructuring. HSBC was not immune from the turmoil. Our pre-tax profit of US$10.2 billion was 28 per cent lower than in the first half of 2007. In the prevailing market conditions this is a resilient performance which enables us to maintain our capital strength, continue with our dividend policy and balance the need to conserve capital with our commitment to make it available for investment in our fast-growing businesses.

The Directors have approved a second interim dividend of US$0.18 per share, an increase of 6 per cent, which is payable on 8 October with a scrip alternative.

Resilient operating performance in the first half of 2008

In the first half of 2008 we remained profitable in all our customer groups. We also remained profitable in all of our geographical regions with the continuing exception of North America. Revenue rose by 3 per cent compared with the first half of 2007; loan impairments were up by 58 per cent but were 8 per cent lower than in the second half. Costs on an underlying basis were well contained, growing by only 4 per cent compared with the first half of 2007 and down by 2 per cent on the second half.

Compared with the second half of 2007, we improved profitability in all our customer groups and for the Group as a whole by 2 per cent. In particular, it is notable that profitability in Global Banking and Markets where extremely difficult market conditions led to writedowns of US$3.9 billion was 37 per cent higher than in the second half of 2007. Meanwhile, our US consumer finance business continued to face difficulties, but performed within our expectations, with loan impairments of US$6.6 billion, lower than in the second half of 2007 by 17 per cent. The Group Chief Executive s Review covers our operational performance in more detail.

Financial strength maintained

HSBC s commitment to maintaining its financial strength is unwavering. HSBC remains both strongly capitalised and liquid. The tier 1 capital ratio was 8.8 per cent and tier 1 capital grew by US$6.2 billion during the period. We have maintained our key credit ratings, generated good profitability in adverse market conditions and continued to focus investment on our strategic priorities.

Our principal concerns in this environment have been risk management, strict cost control, supporting our customers and continued investment to support our long-term strategic ambitions. Our broad-based and resilient revenue streams continue to provide a stable platform from which to achieve strong, long-term performance.

Strategic changes to HSBC s shape

The sale of the regional bank network in France to Banque Populaire announced in February was completed on 2 July and a gain of US$2.1 billion will be recorded in our second half results. The HSBC business in France is now concentrated in France s major urban areas, particularly Paris; the business is focused primarily on Global Banking and Markets, Premier, private banking and commercial banking, specifically for businesses involved in international markets.

We acquired the assets, liabilities and operations of The Chinese Bank in Taiwan in March, adding 36 branches and over one million customers to our operations in Asia s fourth-largest banking market. In May, we announced an agreement to acquire 73.21 per cent of IL&FS Investsmart Ltd, a leading retail brokerage in India, for a total consideration of around US$260 million, giving us a securities presence alongside our banking and insurance businesses in Asia s third largest economy.

Turbulent environment

The economic and financial environment deteriorated progressively through the first half of the year . In the major developed economies where we operate, economic growth slowed as asset prices, particularly of residential property, declined; this in turn affected consumer confidence and hence spending. In credit markets, illiquidity remained a major issue, with trading volumes low and no sign of resumption of normal activity levels in the securitisation markets. As a consequence, the banking system continued to deleverage, putting further pressure on asset prices and raising credit default risk.

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Group Chairman s Statement (continued)

In the emerging markets, where HSBC is the leading international bank, growth remained strong in the period as real asset prices continued to rise and infrastructure development continued to boost economic growth, which supported consumer confidence and spending. However, a number of these economies are now facing increasing inflationary pressures as their consumption of commodities, energy and foodstuffs grows.

Slowing global economy

The outlook for the near term remains highly challenging with significant uncertainty. Globally, consumer confidence is declining and despite the short-term success of the recent fiscal stimulus, the US economy continues to be weak, driven by continuing housing market difficulties. The UK and other economies in Europe which had enjoyed housing market booms, have also weakened. The decline in credit availability is accelerating this process.

We expect growth in emerging markets will hold up reasonably well, albeit with less momentum than in the recent past. In Asia, compared with the buoyant conditions of last year, it is apparent that corporate activity in some sectors is slowing and demand for equity-related and wealth products has reduced as equity markets have declined.

Positioning HSBC for long-term growth

It is clear that growth models in our industry based on high and increasing leverage will no longer be sustainable. It is also clear that complexity in financial services and the recent consequences of failed risk management need to be addressed. Along with its supervisors, our industry including lenders, underwriters and investors needs to reflect on the lessons for risk management, capital adequacy and funding. Ultimately, the real economy will recover from this crisis, although it may get worse before it gets better. Financial markets will not, and should not, return to the *status quo ante*.

Through this period of major uncertainty and beyond, we will continue to position HSBC for long-term growth. The major global long-term trends the key drivers of change which underline our strategic thinking remain intact. Emerging markets will grow faster than mature ones; world trade and investment will grow faster than world GDP; and the ageing of the world s population continues. All of these trends have significant implications for financial services.

We will continue to build HSBC s platform to serve our customers as these trends shape their societies, their businesses and their own needs. We will focus investment primarily on the faster growing markets and on servicing developed market customers with international connectivity. Our capital and balance sheet strength, and a commitment to strict cost control, will continue to underpin our performance.

While the near term poses real uncertainties and difficulties, it may also create opportunities for HSBC to accelerate the execution of our strategy. In a stressed environment, HSBC has the advantages of a powerful brand, a strong capital and funding position, and the ability to service our international customers around the world. We continue to have the capacity to deploy capital at a time when others may be constrained. The strength of our funding base means that, in many markets, we have an opportunity to attract new customers and deliver more for existing ones. We take a long-term view of our business and our customer relationships; we believe that this is the basis for sustainable long-term performance for our shareholders. We will never depart from this. With 335,000 colleagues, we will continue to serve our over 100 million customers around the world, working to fulfil their financial needs.

Stephen Green, *Group Chairman*
4 August 2008

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Group Chief Executive s Review

Resilient performance in a challenging environment

HSBC is the world s local bank . And we are the world s leading international bank in emerging markets. This gives us the opportunity to create value by focusing on faster growing markets, moving towards 60 per cent of our pre-tax profit coming from these economies over time. In developed markets, we are focusing both on businesses with international customers where emerging markets connectivity is critical and on businesses with local customers where our global scale means we can create efficiencies for them and us. Finally we have a suite of global products where we have a competitive advantage from scale, expertise and brand.

Our geographic balance and broad customer base is a protection which allowed us, in difficult markets, to achieve a pre-tax profit of US$10.2 billion, albeit 28 per cent lower than in the first half of 2007.

We measure our progress against key performance indicators. Our cost efficiency ratio of 51 per cent was within our range of 48-52 per cent, as we managed the balance between controlling costs and investing in the business.

Our total shareholder return was also on target for the period; top five in our peer group of 27 international banks.

On capital ratios, which reflect HSBC s fundamental commitment to financial strength, our tier 1 ratio remained strong at 8.8 per cent, within the target range of 7.5-9 per cent.

Our return on average total shareholders equity at 12.1 per cent was below our target range of 15 to 19 per cent over the full cycle, but we would expect that in these difficult times.

Expanding Commercial Banking

Commercial Banking is a core business for us and it again performed strongly with pre-tax profit up by

35 per cent to US$4.6 billion. This included a gain of US$425 million from the sale of the UK card-acquiring business to a joint venture with Global Payments Inc. Excluding this, the growth was 22 per cent.

In keeping with our strategy, around 70 per cent of the business growth excluding the card-acquiring gain came from emerging economies, which now account for 54 per cent of Commercial Banking s global profit before tax. Growth was strong in Asia-Pacific, Brazil and the Middle East, reflecting our established positions in these markets, particularly in mainland China, where we are substantially raising our Commercial Banking presence. In addition, profit before tax grew strongly in Brazil as transaction, lending and foreign exchange volumes grew, while loan impairment charges fell.

In the UK, profit before tax grew by 23 per cent, excluding the card acquiring gain, as Commercial Banking continued to expand with strong deposit growth, and increased fee income from card-issuing and foreign-exchange initiatives. Despite a 13 per cent growth in lending, we kept loan impairment charges in the UK broadly unchanged. In North America, profitability was affected by the slowing economy and by market interest rates. Loan impairment charges increased in both the US and Canada, while in the US and Bermuda, net interest income on liabilities was adversely affected by lower US dollar interest rates.

Commercial Banking grew its small business customer base by 8 per cent to 2.9 million, with particular growth in Turkey, Taiwan, India and mainland China. We are committed to the small business sector as a profit-growth opportunity, a strong source of deposits and fee income.

More and more of our commercial customers are now using our Business Direct service to do their banking online and by telephone. Since its launch in the UK two years ago, and in Brazil last year, over 150,000 businesses have signed up. We will launch in India and Northern Ireland in the second half.

We recognise that our particular advantage in the commercial markets sector is our ability to grow our cross-border income by being where our customers are, participating at both ends of international transactions. Our Commercial Banking revenues are growing at over four times the rate of world trade.

We are further developing our Global Links customer referral system, and cross-border referrals increased by 126 per cent to over 2,700. The

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Group Chief Executive s Review (continued)

aggregate value of these transactions increased by 83 per cent to US$5.6 billion. We continue to join up across functions, with revenues of Global Markets foreign exchange increasing by 44 per cent, and Commercial Banking referrals to Private Banking increasing net new money by 80 per cent.

Personal Financial Services: continued difficulties in the US, strength elsewhere

Profit before tax in Personal Financial Services fell by 51 per cent to US$2.3 billion. This was largely due to the higher loan impairment charges in the US consumer finance business. Elsewhere, the business performed strongly, with pre-tax profits excluding US consumer finance up by 23 per cent.

In emerging markets, we had a very strong six months. We maintained revenue momentum in Rest of Asia-Pacific as well as building out our branch network, with 63 new branches, notably in Greater China. We grew our business in the Middle East profitably on the back of balance sheet growth, and in Latin America with an increased share of credit cards in Mexico and strong deposit growth in Brazil.

We strengthened our position in the UK mortgage market with our successful RateMatcher campaign. Market share of new mortgage lending rose from 3 per cent in the first half of 2007 to 6 per cent in 2008, peaking at 12 per cent in May. We also grew our international customer base in France, through our Investor Services unit.

As part of our Joining up the company strategy, we are focusing on attracting the affluent, high end, internationally mobile personal customers who we believe HSBC suits best. HSBC Premier was designed with these customers in mind. We attracted 208,000 new customers in the first half and now have close to 2.4 million in total. We are on track to achieve 2.6 million Premier customers by the end of the year.

We originally estimated that half of these customers would be new to HSBC but, in the period, over 80 per cent were new to the bank. Each customer generates an average annualised revenue of over US$2,000. This is further evidence that Joining up the company is creating new revenue streams.

HSBC Direct, our online banking system, is also ahead of our expectations. In the face of the industry's desire to raise core deposits, we experienced stiff competition, particularly in the US, and it is testimony to our brand's strength that despite this, we increased our customer base by 15 per cent to 1.2 million customers and grew total deposits by 19 per cent to US$16.1 billion. The

intrinsic value of HSBC Direct will increase further as we begin to achieve cross-sales of other products to these customers.

We continued to expand One HSBC Cards, our global cards platform. In emerging markets, card growth was 5 per cent.

Personal Financial Services US update

In the US, our Personal Financial Services business made a loss of US$2.2 billion. Loan impairment charges and other credit risk provisions rose by 85 per cent on the first half of 2007 to US$6.8 billion, but declined by 15 per cent compared with the second half. The US remains a difficult market, with rising unemployment and falling house prices, and we have recognised this with an impairment charge of US$527 million on the goodwill of our North American Personal Financial Services businesses at Group level.

We continued to take decisive action to mitigate our position. In the first half of 2008, excluding goodwill impairment, we reduced costs by 12 per cent compared with the first half of 2007. We continued to shrink the consumer lending branch network, from 1,000 to 900 branches.

Today, we have announced the run-off of our vehicle finance business. Our vehicle finance portfolio actually improved credit quality over the period but the business does not have sufficient critical mass or the pricing power to provide an acceptable return to the Group, and so we will not be originating further loans. We expect an orderly runoff of about 80 per cent of the portfolio of US$13 billion to be achieved in 3 years, with the remaining balance trailing off after that time.

Our US-based consumer finance business will now be focused mainly on cards and consumer lending.

In mortgage services, we reduced the portfolio outstandings by 13 per cent during the period, down from US$36 billion to US$31 billion, of which around 60 per cent was from repayments.

Emerging markets strength in Global Banking and Markets

Global Banking and Markets made a pre-tax profit of US$2.7 billion, down 35 per cent over the first half of 2007 but 37 per cent higher than in the second half. In emerging markets, profit before tax was up by 51 per cent.

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We wrote down US$3.9 billion on credit trading, monoline exposures and leveraged acquisition financing loans. This reflected the effect of market illiquidity across all asset-backed and structured-product sectors. HSBC s exposure to illiquid markets and the consequent uncertainty over mark-to-market values remains modest with only 3 per cent of our assets having to be valued with reference to significant unobservable price inputs. We have no material exposure to collateralised debt obligations backed by US sub-prime mortgages.

In the half, we created a stable funding basis for our Structured Investment Vehicles (SIVs) by establishing new securities investment conduits. Since the end of 2007, assets held by the SIVs and the new conduits and consolidated on HSBC s balance sheet have declined by US$11 billion to US$29 billion, primarily as assets have been sold or run off.

Our foreign exchange business reported record revenues. The gains reflected greater market volatility and higher customer volumes. Strong results were seen in Rates where increased customer activity and growth in deal volumes increased income.

Global Transaction Banking operates across Commercial Banking and Global Banking and Markets. It generated US$4.6 billion of revenue in the first half of 2008, up by US$0.7 billion. Payments and cash management revenues were 10 per cent ahead of the first half of 2007, the strong liability growth offsetting the effect of declining spreads following rate cuts. Trade and supply chain performed strongly, increasing by 27 per cent despite retail weakness in the US and the UK.

We continued to concentrate on Global Banking and Markets emerging markets-led and financing-focused strategy. The relevance of that cross-border strategy and the strength of HSBC s corporate and institutional franchise was illustrated by the number of transactions in which we acted on behalf of our clients. In the first half of 2008, HSBC acted for more than 700 clients in 29 sectors in some 60 countries. The notional value of these transactions amounted to more than a trillion US dollars.

Recognition for what has been achieved included being awarded Best Emerging Market Bank by *Euromoney.* We closed a number of landmark cross-border deals, including Vale's US$12.2 billion global equity offering, the largest ever follow-on offering by a Latin American company. We advised Ford on the US$2.3 billion sale of its Jaguar and Land Rover businesses to Tata Motors and we were

sole book runner of PetroRabigh s US$1.2 billion IPO, the first IPO by a Saudi Aramco affiliate.

Expanding Private Banking in emerging markets

Private Banking pre-tax profits increased by 5 per cent to US$822 million, primarily due to strong performances in Switzerland and Monaco. In difficult times, we increased total client assets by 1 per cent in the first half of 2008 to US$499 billion. Private Banking generates 59 per cent of its business from clients in emerging markets. We have recently opened three new Private Banking offices in mainland China.

Overall, referrals to Private Banking from other customer groups have increased by 28 per cent. Net new money from referrals is up over 70 per cent, to US$3.4 billion.

Building our insurance proposition

We continue to develop our insurance business worldwide, which now represents 16 per cent of the Group s pre-tax profit. Premium growth was up by 30 per cent, driven mainly by Latin America, Hong Kong and Europe.

Insurance extended its reach with the start of operations in India and the launch of our joint venture in South Korea. Our Preferred Strategic Providers now operate in 23 countries with 82 product launches under way, emphasising the power of HSBC s distribution capabilities.

We won several industry awards, including Best Life Insurance Provider in Brazil and *Labels d Excellence* award in France.

Transforming our customers experience by Joining up the company

Joining up the company is about increasing revenues, particularly those which are new to the bank, and slowing cost growth. In previous paragraphs, I have outlined growth coming from Premier, Global Links and Private Banking and we expect this to continue. However, we are also working to develop the synergies that can be achieved by commonality of technology and process through One HSBC , particularly as it relates to reducing our cost base in developed markets. A slowing of the Group's cost growth is evident in our results for this half year.

One HSBC is our programme to re-engineer the company so that wherever possible we use global systems which provide leading customer experience and also drive down the cost of production. For example, One HSBC Call Centre is reducing call

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times for our customers most frequent transactions. One HSBC Collections improves our service and contact capabilities through holistic customer level views versus individual account views. About three-quarters of the Group s global credit card base is now on the One HSBC Cards platform, and in 2008 we will be undertaking conversions in India and Indonesia. Standardising our service proposition under the One HSBC programme has cut our service interruptions in half.

We can now deploy One HSBC systems in a country as a fully integrated package. This is particularly beneficial in our emerging markets as the suite reduces bespoke software costs as well as producing operating benefits. In the first half of 2008, we deployed the One HSBC suite in seven countries (Poland, Brunei, Australia, Russia, Chile, Indonesia and Slovakia). We aim to deploy it in another seven countries in the second half of the year. Migration to our standard One HSBC will play a major part in creating value for customers and shareholders in the coming years. I will update you on our further progress at the year-end.

Continued focus on financial strength

We live in uncertain times, but we have a clear strategy that we are implementing in a focused and effective way. In April, HSBC was named the number one company in the *Forbes* 2000 list of the world s largest companies the first time a non-US company has topped the list. We were also named

the number one bank of *The Banker* s Top 1000 World Banks 2008, for total tier 1 capital.

Our current customers, and our new customers, know we are here to serve and support them, wherever they wish to do business under the HSBC brand in the 85 countries and territories in which we operate.

We know that to extract HSBC s full value for shareholders, we must continue to join up the company for the benefit of all. We have a long way to go, but value can and will be created by staying focused on this objective.

I would like to thank all our 335,000 staff for serving our over 100 million customers and protecting the interests of our 200,000 shareholders by remaining true to the fundamental principles of HSBC.

Michael Geoghegan, *Group Chief Executive*
4 August 2008

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Interim Management Report: Business Review

Principal activities

HSBC is one of the largest banking and financial services organisations in the world, with a market capitalisation of US$185 billion at 30 June 2008.

Through its subsidiaries and associates, HSBC provides a comprehensive range of banking and related financial services. Headquartered in London, HSBC operates through long-established businesses and has an international network of some 11,000 properties in 85 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 or regional banks, typically with large retail deposit bases, and by consumer finance operations.

Strategic direction

HSBC s strategic direction reflects its position as The world s local bank , combining the largest global emerging markets banking business and a uniquely cosmopolitan customer base with an extensive international network and substantial financial strength.

The Group s strategy is aligned with key trends which are shaping the global economy. In particular, HSBC recognises that, over the long term, developing markets are growing faster than the mature economies, world trade is expanding at a greater rate than GDP and life expectancy is lengthening virtually everywhere. Against this backdrop, HSBC s strategy is focused on delivering superior growth and earnings over time by building on the Group s heritage and skills. Its origins in trade in Asia have had a considerable influence over the development of the Group and, as a consequence, HSBC has an established and longstanding presence in many countries. The combination of local knowledge and international breadth is supported by a substantial financial capability founded on balance sheet strength, largely attributable to the scale of the Group s retail deposit bases.

HSBC is progressively reshaping its business by investing primarily in faster growing markets and, in the more developed markets, by focusing on businesses which have international connectivity. Central to these reshaping activities is a policy of maintaining HSBC s capital strength and strong liquidity position.

The Group has identified three main business models for its customer groups and global businesses that embody HSBC s areas of natural advantage:

- businesses with international customers for whom developing markets connectivity is crucial Global Banking and Markets, Private Banking, the large business segment of Commercial Banking and the mass affluent segment of Personal Financial Services;
- businesses with local customers where efficiency can be enhanced through global scale the small business segment of Commercial Banking and the mass market segment of Personal Financial Services; and
- products where global scale is possible through building efficiency, expertise and brand global product platforms such as cards and direct banking.

The means of executing the strategy, and further utilising the linkages within the Group, are clear:

- the HSBC brand and global networks will be leveraged to reach new customers and offer further services to existing clients;
- efficiency will be enhanced by taking full advantage of local, regional and global economies of scale, in particular by adopting a common systems architecture wherever possible; and

- objectives and incentives will be aligned to motivate and reward staff for being fully engaged in delivering the strategy.

Reconciliation of reported and underlying profit before tax

HSBC measures its performance internally on a like-for-like basis, eliminating the effects of Group currency translation gains and losses, acquisitions and disposals of subsidiaries and businesses and gains from the dilution of the Group s interests in associates, which distort the period-on-period comparison. HSBC refers to this as its underlying performance.

The tables below show the underlying performance of HSBC for the half-year to 30 June 2008 compared with the half-years to 30 June 2007 and 31 December 2007. Equivalent tables are provided for each of HSBC s customer groups and geographical segments in their respective sections below.

The main differences between HSBC s reported and underlying financial performance were:

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- Foreign currency translation differences were most significant in Europe due to the size of HSBC s operations in the UK. The Group s profit before tax for the first half of 2008 decreased by 28 per cent compared with the first half of 2007. The effect of the change in foreign currency translation rates accounted for an increase of 4 percentage points. The equivalents for the first half of 2008 compared with the second half of 2007 were increases of 2 per cent and 1 per cent, respectively.

- There were a number of acquisitions and disposals that affected both comparisons. The most significant were the acquisitions of

HSBC s partner s share in life insurer, Erisa S. A., and property and casualty insurer, Erisa I. A.R.D. (together now renamed HSBC Assurances) in France in March 2007, and the assets and liabilities of The Chinese Bank in Taiwan in March 2008; and the deemed disposals of the stakes in 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), as a consequence of their making share offerings on the domestic A share market in mainland China in the first half of 2007.

Half-year to 30 June 2008 (1H08) compared with half-year to 30 June 2007 (1H07)

HSBC	1H07 as reported US$m	Disposals and dilution gains[1] US$m	Currency translation[2] US$m	1H07 at 1 H08 exchange rates US$m	Acquisitions[1] US$m	Underlying change US$m	1H08 as reported US$m	Reported change %	Underlying change %
Net interest income	18,230	(7)	587	18,810	158	2,210	21,178	16	12
Net fee income	10,495	70	351	10,916	(45)	120	10,991	5	1
Other income[3]	9,768	(1,177)	393	8,984	(45)	(1,633)	7,306	(25)	(18)
Net operating income[4]	38,493	(1,114)	1,331	38,710	68	697	39,475	3	2
Loan impairment charges and other credit risk provisions	(6,346)		(124)	(6,470)		(3,588)	(10,058)	(58)	(55)
Net operating income	32,147	(1,114)	1,207	32,240	68	(2,891)	29,417	(8)	(9)
Operating expenses	(18,611)	55	(738)	(19,294)	(28)	(818)	(20,140)	(8)	(4)
Operating profit	13,536	(1,059)	469	12,946	40	(3,709)	9,277	(31)	(29)
Income from associates	623		48	671	(12)	311	970	56	46
Profit before tax	14,159	(1,059)	517	13,617	28	(3,398)	10,247	(28)	(25)

Half-year to 30 June 2008 (1H08) compared with half-year to 31 December 2007 (2H07)

Disposals 2H07

HSBC	2 H07 as reported US$m	and dilution gains[1] US$m	Currency translation[2] US$m	at 1H08 exchange rates US$m	Acqui-sitions[1] US$m	Under-lying change US$m	1H08 as reported US$m	Re-ported change %	Under-lying change %
Net interest income	19,565	(5)	213	19,773	8	1,397	21,178	8	7
Net fee income	11,507	(52)	98	11,553	1	(563)	10,991	(4)	(5)
Other income[3]	9,428	(15)	16	9,429	4	(2,127)	7,306	(23)	(23)
Net operating income[4]	40,500	(72)	327	40,755	13	(1,293)	39,475	(3)	(3)
Loan impairment charges and other credit risk provisions	(10,896)		(22)	(10,918)		860	(10,058)	8	8
Net operating income	29,604	(72)	305	29,837	13	(433)	29,417	(1)	(1)
Operating expenses	(20,431)	50	(227)	(20,608)	(11)	479	(20,140)	1	2
Operating profit	9,173	(22)	78	9,229	2	46	9,277	1	
Income from associates	880		37	917		53	970	10	6
Profit before tax	10,053	(22)	115	10,146	2	99	10,247	2	1

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Customer groups and global businesses

Summary

HSBC manages its business through two customer groups, Personal Financial Services and Commercial

Banking, and two global businesses, Global Banking and Markets, and Private Banking. Personal Financial Services incorporates the Group s consumer finance businesses.

Profit before tax

	Half-year to					
	30 June 2008		30 June 2007		31 December 2007	
	US$m	**%**	US$m	%	US$m	%
Personal Financial Services	**2,313**	**22.6**	4,729	33.4	1,171	11.7
Commercial Banking	**4,611**	**45.0**	3,422	24.2	3,723	37.0
Global Banking and Markets	**2,690**	**26.2**	4,158	29.4	1,963	19.5
Private Banking	**822**	**8.0**	780	5.5	731	7.3
Other[5]	**(189)**	**(1.8)**	1,070	7.5	2,465	24.5
	10,247	**100.0**	14,159	100.0	10,053	100.0

Total assets6

	At 30 June 2008		At 30 June 2007		At 31 December 2007	
	US$m	**%**	US$m	%	US$m	%
Personal Financial Services	**603,016**	**23.7**	577,402	26.9	588,473	25.0
Commercial Banking	**286,533**	**11.2**	225,763	10.5	261,893	11.1
Global Banking and Markets	**1,509,390**	**59.3**	1,220,316	56.7	1,375,240	58.4
Private Banking	**98,039**	**3.8**	81,916	3.8	88,510	3.8
Other	**49,700**	**2.0**	45,044	2.1	40,150	1.7
	2,546,678	**100.0**	2,150,441	100.0	2,354,266	100.0

For footnotes, see page 89.

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.

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Personal Financial Services

Profit before tax

	Half-year to		
	30 June 2008 US$m	30 June 2007 US$m	31 December 2007 US$m
Net interest income	**15,217**	13,998	15,071
Net fee income	**5,626**	5,523	6,219
Trading income excluding net interest income	**142**	1	37
Net interest income on trading activities	**42**	92	48
Net trading income[7]	**184**	93	85
Net income/(expense) from financial instruments designated at fair value	**(1,135)**	796	537
Gains less losses from financial investments	**585**	60	291
Dividend income	**15**	41	14
Net earned insurance premiums	**4,746**	3,735	4,536
Other operating income	**390**	255	132
Total operating income	**25,628**	24,501	26,885
Net insurance claims[8]	**(3,206)**	(3,605)	(4,542)
Net operating income[4]	**22,422**	20,896	22,343
Loan impairment charges and other credit risk provisions	**(9,384)**	(5,928)	(10,244)
Net operating income	**13,038**	14,968	12,099
Total operating expenses	**(11,099)**	(10,452)	(11,305)
Operating profit	**1,939**	4,516	794
Share of profit in associates and joint ventures	**374**	213	377
Profit before tax	**2,313**	4,729	1,171
By geographical region			
Europe	**1,324**	604	977
Hong Kong	**2,036**	1,898	2,314
Rest of Asia-Pacific	**535**	351	409
North America	**(2,050)**	1,488	(3,034)

Latin America	**468**	388	505
Profit before tax	**2,313**	4,729	1,171
	%	%	%
Share of HSBC s profit before tax	**22.6**	33.4	11.7
Cost efficiency ratio	**49.5**	50.0	50.6

Balance sheet data[6]

	US$m	US$m	US$m
Loans and advances to customers (net)	**458,302**	460,196	464,726
Total assets	**603,016**	577,402	588,473
Customer accounts	**474,263**	416,525	450,071

For footnotes, see page 89.

Business highlights

- Profit before tax in Personal Financial Services was US$2.4 billion lower than that reported in the first half of 2007 and was 53 per cent lower on an underlying basis, primarily because of higher loan impairment charges in the US consumer finance business. Excluding this business, pre-tax profits rose by 23 per cent, 18 per cent on an underlying basis. Compared with the second half of 2007, on an underlying basis, profit before tax in Personal Financial Services was 89 per cent higher as both loan impairment charges and operating expenses fell.

- Market turmoil in the first half of 2008 led retail customers to move their assets from investment products into bank deposits and concentrate their savings in the largest and best regarded financial institutions. HSBC benefited from both these trends with customer accounts growing by US$24.2 billion or 5 per cent in the period.

- HSBC Premier (Premier), the Group s global banking service which offers affluent customers a seamless international service, continued to build on the success of its relaunch in 2007. In the first half of 2008, the service was extended to a further four countries, with a fifth added in July, taking the total to forty. 208,000 net new customers joined Premier, of whom more than 80 per cent were new to the Group. At 30 June 2008, HSBC had 2.4 million Premier customers who, on average, each generated more than US$2,000 of annualised revenues.

- HSBC Direct, the Group s online banking product suite, continued to expand in the four markets in which the product has been launched to date. In aggregate, HSBC Direct balances reached US$16.1 billion and customer numbers 1.2 million, increases of 19 per cent and 15 per cent, respectively, from 31 December 2007.

- HSBC s focus on emerging markets was reflected in growth in cards in force of 5 per cent in these countries compared with 31 December 2007.

- In the UK, HSBC successfully launched a RateMatcher promotion to attract higher quality customers facing an interest rate reset in the near term. In the three months of the offer, HSBC attracted a strong flow of new business, both for the RateMatcher product and other mortgages. Overall, HSBC attracted US$11 billion of balances during the campaign.

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- Notwithstanding weaker equity markets in Asia, HSBC s Personal Financial Services businesses in both Hong Kong and Rest of Asia-Pacific maintained revenue momentum, with notable success in deposit generation, particularly from Premier customers.

- Consistent with HSBC s strategy to increase the sale of insurance products to existing customers, underlying net premium income and insurance fee income grew by 7 per cent and 18 per cent, respectively.

- In the US, declining house prices, together with a continuing reduction in the availability of mortgage finance, fuelled growing customer delinquencies as house price depreciation became more pronounced and the economy weakened. HSBC continued to take measures to help customers manage their mortgage repayments and avoid foreclosure. In the first half of 2008, HSBC Finance extended its mortgage loan modification programme, with longer term modifications. Some 90 per cent of US mortgage customers remained current, or only one payment overdue, across the consumer lending business. Normal repayments and continued write-offs lowered the mortgage services portfolio by US$4.8 billion to US$31.4 billion at 30 June 2008.

Reconciliation of reported and underlying profit before tax

Half-year to 30 June 2008 (1H08) compared with half-year to 30 June 2007 (1H07)

Personal Financial Services	**1H07 as reported US$m**	**Disposals and dilution gains[1] US$m**	**Currency translation[2] US$m**	**1H07 at 1H08 exchange rates US$m**	**Acquisitions[1] US$m**	**Underlying change US$m**	**1H08 as reported US$m**	**Reported change %**	**Underlying change %**
Net interest income	**13,998**	**(7)**	**397**	**14,388**	**156**	**673**	**15,217**	**9**	**5**
Net fee income	**5,523**	**122**	**136**	**5,781**	**(45)**	**(110)**	**5,626**	**2**	**(2)**
Other income[3]	**1,375**	**(101)**	**48**	**1,322**	**(47)**	**304**	**1,579**	**15**	**23**
Net operating income[4]	**20,896**	**14**	**581**	**21,491**	**64**	**867**	**22,422**	**7**	**4**
Loan impairment charges and other credit risk provisions	**(5,928)**		**(104)**	**(6,032)**		**(3,352)**	**(9,384)**	**(58)**	**(56)**
Net operating income	**14,968**	**14**	**477**	**15,459**	**64**	**(2,485)**	**13,038**	**(13)**	**(16)**
Operating expenses	**(10,452)**	**5**	**(395)**	**(10,842)**	**(25)**	**(232)**	**(11,099)**	**(6)**	**(2)**
Operating profit	**4,516**	**19**	**82**	**4,617**	**39**	**(2,717)**	**1,939**	**(57)**	**(59)**
Income from associates	**213**		**18**	**231**		**143**	**374**	**76**	**62**
Profit before tax	**4,729**	**19**	**100**	**4,848**	**39**	**(2,574)**	**2,313**	**(51)**	**(53)**

Half-year to 30 June 2008 (1H08) compared with half-year to 31 December 2007 (2H07)

Personal Financial Services	2H07 as reported US$m	Disposals and dilution gains[1] US$m	Currency translation [2] US$m	2H07 at 1H08 exchange rates US$m	Acquisitions[1] US$m	Underlying change US$m	1H08 as reported US$m	Reported change %	Underlying change %

Net interest income	15,071	(5)	133	15,199	6	12	15,217	1	
Net fee income	6,219		25	6,244	1	(619)	5,626	(10)	(10)
Other income[3]	1,053	19	16	1,088	2	489	1,579	50	45
Net operating income[4]	22,343	14	174	22,531	9	(118)	22,422		(1)
Loan impairment charges and other credit risk provisions	(10,244)		(25)	(10,269)		885	(9,384)	8	9
Net operating income	12,099	14	149	12,262	9	767	13,038	8	6
Operating expenses	(11,305)	2	(131)	(11,434)	(9)	344	(11,099)	2	3
Operating profit	794	16	18	828		1,111	1,939	144	134
Income from associates	377		19	396		(22)	374	(1)	(6)
Profit before tax	1,171	16	37	1,224		1,089	2,313	98	89

For footnotes, see page 89.

Commercial Banking

Profit before tax

	Half-year to		
	30 June 2008 US$m	30 June 2007 US$m	31 December 2007 US$m
Net interest income	**4,747**	4,286	4,769
Net fee income	**2,165**	1,904	2,068
Trading income excluding net interest income	**197**	121	144
Net interest income on trading activities	**24**	13	18
Net trading income[7]	**221**	134	162
Net income/(expense) from financial instruments designated at fair value	**(59)**	(24)	46
Gains less losses from financial investments	**191**	25	65
Dividend income	**3**	4	4
Net earned insurance premiums	**360**	205	528
Other operating income	**718**	2	163
Total operating income	**8,346**	6,536	7,805
Net insurance claims[8]	**(190)**	44	(435)
Net operating income[4]	**8,156**	6,580	7,370
Loan impairment charges and other credit risk provisions	**(563)**	(431)	(576)
Net operating income	**7,593**	6,149	6,794
Total operating expenses	**(3,280)**	(2,907)	(3,345)
Operating profit	**4,313**	3,242	3,449
Share of profit in associates and joint ventures	**298**	180	274
Profit before tax	**4,611**	3,422	3,723
By geographical region			
Europe	**1,940**	1,236	1,280
Hong Kong	**869**	760	859
Rest of Asia-Pacific	**961**	597	753
North America	**430**	477	443

Latin America	**411**	352	388
Profit before tax	**4,611**	3,422	3,723
	%	%	%
Share of HSBC s profit before tax	**45.0**	24.2	37.0
Cost efficiency ratio	**40.2**	44.2	45.4

Balance sheet data[6]

	US$m	US$m	US$m
Loans and advances to customers (net)	**238,116**	185,923	220,068
Total assets	**286,533**	225,763	261,893
Customer accounts	**247,705**	205,002	237,987

For footnotes, see page 89.

Business highlights

- Pre-tax profits increased by 35 per cent to US$4.6 billion. This included a gain of US$425 million from selling the Group s merchant acquiring business in the UK to a new card processing joint venture with Global Payments Inc. Operating performance was driven by robust growth in economic activity in developing markets, where much of the Group s incremental credit appetite was directed. This led to strong revenue generation with costs rising at approximately half the rate of income as productivity improved. Loan impairment charges rose as economic conditions weakened during the first half of 2008.

- Pre-tax profits in Europe, including the gain from the new card processing joint venture, were 57 per cent higher. Growth in profit was strongest in the Middle East and Asia-Pacific, reflecting the Group s established position in these fast- growing economies. Growth was also strong in Brazil. Underlying income and profit fell in North America, largely as a result of increased loan impairment charges.

- Excluding the gain on the sale of the merchant acquiring business, the share of Commercial Banking s profit from developing markets rose from 52 per cent in 2007 to 54 per cent in the first half of 2008.

- Strong revenue growth of 29 per cent from trade and supply chain and 44 per cent from foreign exchange reflected Commercial Banking s leading international business strategy. HSBC has benefited from growth in intra-regional trade flows and from facilitating investment flows from developed to developing economies, in part utilising its network of International Business Centres. Cross-border referrals through the Global Links system in the first half of 2008 rose by over 126 per cent in number and by over 83 per cent in aggregate transaction value compared with the first half of 2007.

- The best bank for small business strategy also contributed strongly to income growth, with an increase in deposits gathered from small business customers. Total customer numbers grew by 8 per cent to 2.9 million, largely among small and micro-business customers. Dedicated small- business centres in Turkey and the success of BusinessDirect in the UK contributed to this growth.

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- Both physical and online distribution capabilities were expanded. In Turkey, the number of Small Business Centres was increased to over 100 and in the UK local business managers were redeployed to key branches. In Taiwan, the acquisition of the assets, liabilities and operations of The Chinese Bank extended HSBC s reach, the additional branches bringing the total number to 44. At 8,300, the total number of relationship managers was 20 per cent higher than at 30 June 2007, with particularly strong growth in India following implementation of a new small business strategy.
- The number of small and micro business customers using business internet banking increased by 22 per cent to nearly 900,000; the number of mid-market and corporate customers rose by 28 per cent to over 35,000.
- Referrals to other customer groups and global businesses increased, specifically mortgages and Premier referrals to Personal Financial Services, debt and advisory services, to Global Banking and Markets, and ongoing referrals to Private Banking.

Reconciliation of reported and underlying profit before tax

Half-year to 30 June 2008 (1H08) compared with half-year to 30 June 2007 (1H07)

Commercial Banking	**1H07 as reported US$m**	**Disposals and dilution gains[1] US$m**	**Currency translation[2] US$m**	**1H07 at 1H08 exchange rates US$m**	**Acqui-sitions[1] US$m**	**Under-lying change US$m**	**1H08 as reported US$m**	**Re-ported change %**	**Under-lying change %**
Net interest income	**4,286**		**195**	**4,481**	**3**	**263**	**4,747**	**11**	**6**
Net fee income	**1,904**		**75**	**1,979**		**186**	**2,165**	**14**	**9**
Other income[3]	**390**		**14**	**404**	**2**	**838**	**1,244**	**219**	**207**
Net operating income[4]	**6,580**		**284**	**6,864**	**5**	**1,287**	**8,156**	**24**	**19**
Loan impairment charges and other credit risk provisions	**(431)**		**(17)**	**(448)**		**(115)**	**(563)**	**(31)**	**(26)**
Net operating income	**6,149**		**267**	**6,416**	**5**	**1,172**	**7,593**	**23**	**18**
Operating expenses	**(2,907)**		**(157)**	**(3,064)**	**(2)**	**(214)**	**(3,280)**	**(13)**	**(7)**
Operating profit	**3,242**		**110**	**3,352**	**3**	**958**	**4,313**	**33**	**29**
Income from associates	**180**		**11**	**191**		**107**	**298**	**66**	**56**
Profit before tax	**3,422**		**121**	**3,543**	**3**	**1,065**	**4,611**	**35**	**30**

Half-year to 30 June 2008 (1H08) compared with half-year to 31 December 2007 (2H07)

Commercial Banking	2H07 as reported US$m	Disposals and dilution gains[1] US$m	Currency translation[2] US$m	2H07 at 1H08 exchange rates US$m	Acqui-sitions[1] US$m	Under-lying change US$m	1H08 as reported US$m	Re-ported change %	Under-lying change %
Net interest income	4,769		50	4,819	3	(75)	4,747		(2)

Net fee income	2,068		13	2,081		84	2,165	5	4
Other income[3]	533		(4)	529	2	713	1,244	133	135
Net operating income[4]	7,370		59	7,429	5	722	8,156	11	10
Loan impairment charges and other credit risk provisions	(576)		2	(574)		11	(563)	2	2
Net operating income	6,794		61	6,855	5	733	7,593	12	11
Operating expenses	(3,345)		(50)	(3,395)	(2)	117	(3,280)	2	3
Operating profit	3,449		11	3,460	3	850	4,313	25	25
Income from associates	274		9	283		15	298	9	5
Profit before tax	3,723		20	3,743	3	865	4,611	24	23

For footnotes, see page 89.

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Global Banking and Markets

Profit before tax

	Half-year to		
	30 June 2008 US$m	30 June 2007 US$m	31 December 2007 US$m
Net interest income	**3,737**	1,847	2,583
Net fee income	**2,354**	2,264	2,637
Trading income excluding net interest income	**360**	3,048	455
Net interest income/(expense) on trading activities	**273**	(151)	(85)
Net trading income[7]	**633**	2,897	370
Net income/(expense) from financial instruments designated at fair value	**(211)**	11	(175)
Gains less losses from financial investments	**244**	768	545
Dividend income	**49**	175	47
Net earned insurance premiums	**62**	46	47
Other operating income	**551**	529	689
Total operating income	**7,419**	8,537	6,743
Net insurance claims[8]	**(40)**	(38)	(32)
Net operating income[4]	**7,379**	8,499	6,711
Net loan impairment (charges)/recoveries and other credit risk provisions	**(115)**	24	(62)
Net operating income	**7,264**	8,523	6,649
Total operating expenses	**(4,827)**	(4,479)	(4,879)
Operating profit	**2,437**	4,044	1,770
Share of profit in associates and joint ventures	**253**	114	193
Profit before tax	**2,690**	4,158	1,963
By geographical region			
Europe	**1,190**	1,674	853
Hong Kong	**770**	697	881
Rest of Asia-Pacific	**1,972**	1,098	1,366
North America	**(1,625)**	436	(1,401)
Latin America	**383**	253	264

Profit before tax	**2,690**	4,158	1,963
	%	%	%
Share of HSBC s profit before tax	**26.2**	29.4	19.5
Cost efficiency ratio	**65.4**	52.7	72.7

For footnotes, see page 89.

Business highlights

- In the most difficult financial market conditions seen for many decades, Global Banking and Markets delivered pre-tax profits of US$2.7 billion, an improvement of US$727 million or 37 per cent on the six months ended 31 December 2007 but some US$1.5 billion lower than in the first half of 2007.

- The result reflected a total of US$3.9 billion of write-downs on credit trading, leveraged and acquisition financing positions and monoline credit exposures resulting from the continued deterioration in the credit markets. This compared with US$2.1 billion for the second half of 2007 and nil for the first half of 2007. Partly offsetting this was a US$262 million fair value gain on the widening of credit spreads on structured liabilities.

- Notwithstanding the challenging market conditions in credit trading and Principal Investments, where the opportunities to realise assets diminished in 2008, other businesses performed very well. The emerging markets-led and financing-focused strategy continued to ensure that HSBC was well positioned to support clients as they undertook cross-border transactions into and out of emerging markets.

- In Global Markets, the foreign exchange business reported record revenues. This reflected greater market volatility and higher customer volumes.

- Strong results were seen in Rates, where increased customer activity and growth in deal volumes resulted in income rising by 120 per cent. In equities, excluding the effect of the gain on sale of HSBC s investment in Euronext N.V and the Montreal Exchange in 2007, revenues rose by 37 per cent.

- The securities services business continued to grow despite the backdrop of lower interest rates and lower equity markets, as stronger transaction volumes and new mandates resulted in higher revenues. This was particularly evident in Asia, as clients continued to rebalance their investment portfolios.

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Management view of total operating income

	Half-year to		
	30 June 2008 US$m	30 June 2007 US$m	31 December 2007 US$m
Global Markets	**1,688**	3,825	1,895
Credit	**(3,124)**	658	(1,977)
Rates	**1,303**	592	699
Foreign exchange	**1,546**	909	1,269
Equities[10]	**746**	652	525
Securities services	**1,112**	855	1,071
Asset and structured finance	**105**	159	308
Global Banking	**2,432**	1,974	2,216
Financing and equity capital markets	**1,371**	1,042	1,144
Payments and cash management	**839**	751	881
Other transaction services	**222**	181	191
Balance Sheet Management	**1,630**	521	705
Global Asset Management	**669**	636	700
Principal Investments	**167**	755	498
Other[11]	**833**	826	729
Total operating income	**7,419**	8,537	6,743

Balance sheet data[6]

Trading assets (including derivatives)	**721,366**	567,340	625,132
Trading liabilities (including derivatives)	**577,048**	443,634	483,881
Financial investments	**211,486**	174,095	224,057
Financial assets designated at fair value	**7,469**	5,269	7,936
Loans and advances to:			
customers (net)	**303,826**	241,602	250,464
banks (net)	**214,693**	183,708	199,506
Total assets	**1,509,390**	1,220,316	1,375,240
Customer accounts	**328,952**	265,739	299,879
Deposits by banks	**144,043**	121,744	126,395

Comparative information has been restated to reflect the current management view.

In the first half of 2008, Global Markets included a US$262 million fair value gain on the widening of credit spreads on structured liabilities.

For footnotes, see page 89.

- Balance Sheet Management recorded significantly higher income from positions taken in expectation of interest rate reductions by a number of central banks. As a result of these positions there was an associated increase in the total value at risk.

- In Global Banking, the write-downs on leveraged and acquisition finance positions were more than offset by gains on credit default swap transactions in other parts of the portfolio. Increased transaction volumes drove robust growth in fees, particularly in emerging markets. Total operating income in payments and cash management was 12 per cent higher, led by a strong rise in deposit balances.

- HSBC s extensive distribution network enabled the delivery of products to emerging markets as recognised by a number of industry awards including Best Investment Bank and Best Risk Management in the Middle East, and Best Debt House in Asia and in Western Europe by *Euromoney.*

- The strength of the Group s corporate and institutional franchise was again illustrated by the number and variety of transactions in which Global Banking acted on behalf of clients. In the first half of 2008, HSBC acted for over 700 clients in 29 sectors and some 60 countries. The total notional transaction value was more than US$1,000 billion.

- Global Asset Management benefited from a significant increase in liquidity fund inflows with total funds under management growing to US$389 billion, as clients sought certainty in a volatile market. The Group maintained its position as one of the leading emerging markets asset managers, with assets increasing to US$86 billion, a rise of 18 per cent on the first half of 2007. The business continued to leverage the Group s distribution capabilities with new funds including HSBC s New Frontiers Fund, launched in February for the Group s Private Banking clients, which raised US$300 million within three months.

- Within the Group s available-for-sale portfolio, continuing illiquidity in asset-backed securities markets led to further write-downs of securities. However, as a consequence of the underlying credit quality and seniority of the tranches held by HSBC, the first half of 2008 included a relatively modest impairment charge through the income statement of US$55 million; a further US$134 million was absorbed by income note holders who take the first loss on positions within the securities investment conduits (SICs) now consolidated in HSBC s accounts. Further details on these SICs are provided on pages 137 to 141.

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Interim Management Report: Business Review (continued)

Reconciliation of reported and underlying profit before tax

Half-year to 30 June 2008 (1H08) compared with half-year to 30 June 2007 (1H07)

Global Banking and Markets	1H07 as reported US$m	Disposals and dilution gains[1] US$m	Currency translation[2] US$m	1H07 at 1H08 exchange rates US$m	Acquisitions[1] US$m	Underlying change US$m	1H08 as reported US$m	Reported change %	Underlying change %
Net interest income	1,847		72	1,919		1,818	3,737	102	95
Net fee income	2,264		104	2,368		(14)	2,354	4	(1)
Other income[3]	4,388		183	4,571		(3,283)	1,288	(71)	(72)
Net operating income[4]	**8,499**		**359**	**8,858**		**(1,479)**	**7,379**	**(13)**	**(17)**
Loan impairment (charges)/recoveries and other credit risk provisions	24		(2)	22		(137)	(115)	(579)	(623)
Net operating income	**8,523**		**357**	**8,880**		**(1,616)**	**7,264**	**(15)**	**(18)**
Operating expenses	(4,479)		(151)	(4,630)		(197)	(4,827)	(8)	(4)
Operating profit	**4,044**		**206**	**4,250**		**(1,813)**	**2,437**	**(40)**	**(43)**
Income from associates	114		5	119		134	253	122	113
Profit before tax	**4,158**		**211**	**4,369**		**(1,679)**	**2,690**	**(35)**	**(38)**

Half-year to 30 June 2008 (1H08) compared with half-year to 31 December 2007 (2H07)

Global Banking and Markets	2H07 as reported US$m	Disposals and dilution gains[1] US$m	Currency translation[2] US$m	2H07 at 1H08 exchange rates US$m	Acquisitions[1] US$m	Underlying change US$m	1H08 as reported US$m	Reported change %	Underlying change %
Net interest income	2,583		37	2,620		1,117	3,737	45	43
Net fee income	2,637		32	2,669		(315)	2,354	(11)	(12)

Other income[3]	1,491		12	1,503		(215)	1,288	(14)	(14)
Net operating income[4]	6,711		81	6,792		587	7,379	10	9
Loan impairment charges and other credit risk provisions	(62)		2	(60)		(55)	(115)	(85)	(92)
Net operating income	6,649		83	6,732		532	7,264	9	8
Operating expenses	(4,879)		(32)	(4,911)		84	(4,827)	1	2
Operating profit	1,770		51	1,821		616	2,437	38	34
Income from associates	193		8	201		52	253	31	26
Profit before tax	1,963		59	2,022		668	2,690	37	33

For footnotes, see page 89.

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Private Banking

Profit before tax

	Half-year to		
	30 June 2008 US$m	30 June 2007 US$m	31 December 2007 US$m
Net interest income	**783**	567	649
Net fee income	**814**	811	804
Trading income excluding net interest income	**211**	255	270
Net interest income on trading activities	**7**	4	5
Net trading income[7]	**218**	259	275
Net income/(expense) from financial instruments designated at fair value	**1**		(1)
Gains less losses from financial investments	**80**	45	74
Dividend income	**4**	5	2
Other operating income	**16**	31	27
Total operating income	**1,916**	1,718	1,830
Net insurance claims[8]			
Net operating income[4]	**1,916**	1,718	1,830
Loan impairment (charges)/recoveries and other credit risk provisions	**4**	(9)	(5)
Net operating income	**1,920**	1,709	1,825
Total operating expenses	**(1,098)**	(929)	(1,096)
Operating profit	**822**	780	729
Share of profit in associates and joint ventures			2
Profit before tax	**822**	780	731
By geographical region			
Europe	**579**	493	422
Hong Kong	**123**	161	144
Rest of Asia-Pacific	**54**	56	36
North America	**58**	60	114
Latin America	**8**	10	15
Profit before tax	**822**	780	731
	%	%	%
Share of HSBC s profit before tax	**8.0**	5.5	7.3
Cost efficiency ratio	**57.3**	54.1	59.9

Balance sheet data[6]

	US$m	US$m	US$m
Loans and advances to customers (net)	**45,895**	37,863	43,612
Total assets	**98,039**	81,916	88,510
Customer accounts	**109,776**	91,228	106,197

For footnotes, see page 89.

Business highlights

- Pre-tax profits increased by 5 per cent or 4 per cent on an underlying basis to US$822 million, primarily due to strong performances in Switzerland and Monaco, offsetting lower revenues in Asia due to reduced client trading.

- Inward referrals from other customer groups in HSBC in the first half of 2008 resulted in US$3.4 billion of net new money, compared with US$2.0 billion in the first half of 2007.

- Despite a decline in market values, client assets at US$421.3 billion remained well ahead of 30 June 2007 and unchanged from 31 December 2007, assisted by net new money of US$14.5 billion in the first half of 2008. This was achieved with an improvement in net interest income in an environment of competitors offering above-market deposit rates to attract and retain clients. Within client assets, funds and mandates generating annuity income rose by 4 per cent to US$70.3 billion.

Client Assets

	Half-year to		
	30 June 2008 US$bn	30 June 2007 US$bn	31 December 2007 US$bn
At beginning of period	**421**	333	370
Net new money	**15**	17	19
Value change	**(20)**	12	7
Exchange/other	**5**	8	25
At end of period	**421**	370	421

- Total client assets, a measure equivalent to many industry definitions of assets under management, which includes some non-financial assets held in client trusts, amounted to US$499.3 billion at 30 June 2008, an increase of US$5.2 billion on 31 December 2007, including US$18.6 billion of net new money.

- Private Banking clients continued to be attracted to alternative products, with total hedge funds under custody for clients growing to US$57.9 billion, and new product offerings in emerging markets. The HSBC New Frontiers Fund, which concentrates on the next generation emerging markets, and the HSBC Asia Private Equity fund, were notably successful in the first half of 2008.

- Offices in Guangzhou, Shanghai and Beijing were formally opened in early 2008 as part of the launch of Private Banking in mainland China.

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Interim Management Report: Business Review (continued)

Reconciliation of reported and underlying profit before tax

Half-year to 30 June 2008 (1H08) compared with half-year to 30 June 2007 (1H07)

Private Banking	**1H07 as reported US$m**	**Disposals and dilution gains[1] US$m**	**Currency translation[2] US$m**	**1H07 at 1H08 exchange rates US$m**	**Acquisitions[1] US$m**	**Underlying change US$m**	**1H08 as reported US$m**	**Reported change %**	**Underlying change %**
Net interest income	**567**		**9**	**576**		**207**	**783**	**38**	**36**
Net fee income	**811**	**(52)**	**30**	**789**		**25**	**814**		**3**
Other income[3]	**340**		**5**	**345**		**(26)**	**319**	**(6)**	**(8)**
Net operating income[4]	**1,718**	**(52)**	**44**	**1,710**		**206**	**1,916**	**12**	**12**
Loan impairment (charges)/recoveries and other credit risk provisions	**(9)**			**(9)**		**13**	**4**	**144**	**144**
Net operating income	**1,709**	**(52)**	**44**	**1,701**		**219**	**1,920**	**12**	**13**
Operating expenses	**(929)**	**50**	**(33)**	**(912)**		**(186)**	**(1,098)**	**(18)**	**(20)**
Operating profit	**780**	**(2)**	**11**	**789**		**33**	**822**	**5**	**4**
Income from associates									
Profit before tax	**780**	**(2)**	**11**	**789**		**33**	**822**	**5**	**4**

Half-year to 30 June 2008 (1H08) compared with half-year to 31 December 2007 (2H07)

Private Banking	2H07 as reported US$m	Disposals and dilution gains[1] US$m	Currency translation[2] US$m	2H07 at 1H08 exchange rates US$m	Acquisitions[1] US$m	Underlying change US$m	1H08 as reported US$m	Reported change %	Underlying change %
Net interest income	649		2	651		132	783	21	20
Net fee income	804	(52)	18	770		44	814	1	6
Other income[3]	377	(18)	6	365		(46)	319	(15)	(13)
Net operating income[4]	1,830	(70)	26	1,786		130	1,916	5	7
Loan impairment (charges)/recoveries and other credit risk provisions	(5)		(1)	(6)		10	4	180	167

Net operating income	1,825	(70)	25	1,780		140	1,920	5	8
Operating expenses	(1,096)	48	(14)	(1,062)		(36)	(1,098)		(3)
Operating profit	729	(22)	11	718		104	822	13	14
Income from associates	2		(1)	1		(1)		(100)	(100)
Profit before tax	731	(22)	10	719		103	822	12	14

For footnotes, see page 89.

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Other

Profit/(loss) before tax

	Half-year to		
	30 June 2008 US$m	30 June 2007 US$m	31 December 2007 US$m
Net interest expense	**(375)**	(291)	(251)
Net fee income/(expense)	**32**	(7)	(221)
Trading income/(expense) excluding net interest income	**(271)**	(74)	201
Net interest income/(expense) on trading activities	**(82)**	25	(26)
Net trading income/(expense)[7]	**(353)**	(49)	175
Net income from financial instruments designated at fair value	**820**	91	2,802
Gains less losses from financial investments	**(283)**	101	(18)
Gains arising from dilution of interests in associates		1,076	16
Dividend income	**17**	27	5
Net earned insurance premiums	**(15)**	(9)	(12)
Other operating income	**1,943**	1,667	1,856
Total operating income	**1,786**	2,606	4,352
Net insurance claims[8]	**(1)**		
Net operating income[4]	**1,785**	2,606	4,352
Loan impairment charges and other credit risk provisions		(2)	(9)
Net operating income	**1,785**	2,604	4,343
Total operating expenses	**(2,019)**	(1,650)	(1,912)
Operating profit/(loss)	**(234)**	954	2,431
Share of profit in associates and joint ventures	**45**	116	34
Profit/(loss) before tax	**(189)**	1,070	2,465
By geographical region			
Europe	**144**	43	1,013
Hong Kong	**(725)**	(186)	(189)
Rest of Asia-Pacific	**102**	1,242	101
North America	**294**	(26)	1,534
Latin America	**(4)**	(3)	6
Profit/(loss) before tax	**(189)**	1,070	2,465
	%	%	%
Share of HSBC s profit before tax	**(1.8)**	7.5	24.5
Cost efficiency ratio	**113.1**	63.3	43.9

Balance sheet data[6]

	US$m	US$m	US$m
Loans and advances to customers (net)	**3,061**	2,517	2,678
Total assets	**49,700**	45,044	40,150
Customer accounts	**1,227**	2,338	2,006

For footnotes, see page 89.

Notes

- The loss before tax recorded in Other, US$189 million, was US$1,259 million less than the profit of US$1,070 million in the first half of 2007. For a description of the main items reported under Other , please see footnote 5 on page 89.

- Net income from financial instruments designated at fair value of US$820 million was recorded in the first half of 2008. This represented nearly a nine-fold increase on the first half of 2007 and arose principally from mark-to-market gains driven by wider credit spreads from fair valuing own debt issued by HSBC Holdings and its European and North American subsidiaries. These fair value gains will reverse through the income statement over the remaining life of the debt.

- Activities undertaken within the Group Service Centres (GSCs) continued to grow in the first half of 2008. Employee numbers increased by 14 per cent, bringing the total number of people employed by GSCs to over 32,000. In North America, IT Service Centres reported a 3 per cent decrease in costs. Substantially all costs of both GSCs and IT Service Centres are recharged to HSBC s customer groups and global businesses with revenue reported under Other operating income .

- Gains less losses from financial investments included impairment charges of US$296 million recognised on non-trading equity positions classified as available for sale. These investments were made as part of the strategic positioning of HSBC s businesses in Asia, and the write-downs were required as a consequence of significant falls in equity market prices. In the opinion of HSBC management, these stakes continue to deliver the market access envisaged when they were acquired.

- Dilution gains of US$1.1 billion recorded in the first half of 2007 did not recur. These gains were recognised following share offerings made by HSBC s associates: Ping An Insurance, Bank of Communications and Industrial Bank.

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Reconciliation of reported and underlying profit before tax

Half-year to 30 June 2008 (1H08) compared with half-year to 30 June 2007 (1H07)

Other	**1H07 as reported US$m**	**Disposals and dilution gains[1] US$m**	**Currency translation[2] US$m**	**1 H07 at 1 H08 exchange rates US$m**	**Acqui-sitions[1] US$m**	**Under lying change US$m**	**1 H08 as reported US$m**	**Re-ported change %**	**Under-lying change %**
Net interest expense	**(291)**		**(20)**	**(311)**	**(1)**	**(63)**	**(375)**	**(29)**	**(20)**
Net fee income/(expense)	**(7)**		**6**	**(1)**		**33**	**32**	**557**	**3,300**
Other income[3]	**2,904**	**(1,076)**	**104**	**1,932**		**196**	**2,128**	**(27)**	**10**
Net operating income[4]	**2,606**	**(1,076)**	**90**	**1,620**	**(1)**	**166**	**1,785**	**(32)**	**10**
Loan impairment charges and other credit risk provisions	**(2)**		**(1)**	**(3)**		**3**		**100**	**100**
Net operating income	**2,604**	**(1,076)**	**89**	**1,617**	**(1)**	**169**	**1,785**	**(31)**	**10**
Operating expenses	**(1,650)**		**(29)**	**(1,679)**	**(1)**	**(339)**	**(2,019)**	**(22)**	**(20)**
Operating profit/(loss)	**954**	**(1,076)**	**60**	**(62)**	**(2)**	**(170)**	**(234)**	**(125)**	**(274)**
Income from associates	**116**		**14**	**130**	**(12)**	**(73)**	**45**	**(61)**	**(56)**
Profit/(loss) before tax	**1,070**	**(1,076)**	**74**	**68**	**(14)**	**(243)**	**(189)**	**(118)**	**(357)**

Half-year to 30 June 2008 (1H08) compared with half-year to 31 December 2007 (2H07)

Other	2 H07 as reported US$m	Disposals and dilution gains[1] US$m	Currency translation[2] US$m	2 H07 at 1 H08 exchange rates US$m	Acqui-sitions [1] US$m	Under-lying change US$m	1 H08 as reported US$m	Re-ported change %	Under-lying change %
Net interest expense	(251)		(14)	(265)	(1)	(109)	(375)	(49)	(41)
Net fee income/(expense)	(221)		10	(211)		243	32	114	115
Other income[3]	4,824	(16)	2	4,810		(2,682)	2,128	(56)	(56)

Net operating income[4]	4,352	(16)	(2)	4,334	(1)	(2,548)	1,785	(59)	(59)
Loan impairment charges and other credit risk provisions	(9)			(9)		9		100	100
Net operating income	4,343	(16)	(2)	4,325	(1)	(2,539)	1,785	(59)	(59)
Operating expenses	(1,912)		(11)	(1,923)		(96)	(2,019)	(6)	(5)
Operating profit/(loss)	2,431	(16)	(13)	2,402	(1)	(2,635)	(234)	(110)	(110)
Income from associates	34		2	36		9	45	32	25
Profit/(loss) before tax	2,465	(16)	(11)	2,438	(1)	(2,626)	(189)	(108)	(108)

For footnotes, see page 89.

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Analysis by customer group and global business

Profit/(loss) before tax

	Half-year to 30 June 2008						
Total	**Personal Financial Services US$m**	**Commercial Banking US$m**	**Global Banking and Markets US$m**	**Private Banking US$m**	**Other[5] US$m**	**Inter-segment elimination[9] US$m**	**Total US$m**
Net interest income/(expense)	15,217	4,747	3,737	783	(375)	(2,931)	21,178
Net fee income	5,626	2,165	2,354	814	32		10,991
Trading income/(expense) excluding net interest income	142	197	360	211	(271)		639
Net interest income/(expense) on trading activities	42	24	273	7	(82)	2,931	3,195
Net trading income/(expense)[7]	184	221	633	218	(353)	2,931	3,834
Net income/(expense) from financial instruments designated at fair value	(1,135)	(59)	(211)	1	820		(584)
Gains less losses from financial investments	585	191	244	80	(283)		817
Dividend income	15	3	49	4	17		88
Net earned insurance premiums	4,746	360	62		(15)		5,153
Other operating income	390	718	551	16	1,943	(2,183)	1,435
Total operating income	25,628	8,346	7,419	1,916	1,786	(2,183)	42,912
Net insurance claims[8]	(3,206)	(190)	(40)		(1)		(3,437)
Net operating income[4]	22,422	8,156	7,379	1,916	1,785	(2,183)	39,475
Loan impairment (charges)/recoveries and other credit risk provisions	(9,384)	(563)	(115)	4			(10,058)
Net operating income	13,038	7,593	7,264	1,920	1,785	(2,183)	29,417
Total operating expenses	(11,099)	(3,280)	(4,827)	(1,098)	(2,019)	2,183	(20,140)
Operating profit/(loss)	1,939	4,313	2,437	822	(234)		9,277
Share of profit in associates and joint ventures	374	298	253		45		970
Profit/(loss) before tax	2,313	4,611	2,690	822	(189)		10,247
	%	%	%	%	%		%
Share of HSBC s profibefore tax	22.6	45.0	26.2	8.0	(1.8)		100.0
Cost efficiency ratio	49.5	40.2	65.4	57.3	113.1		51.0

Balance sheet data[6]

	U$Sm	US$m	US$m	US$m	US$m		US$m
Loans and advances to customers (net)	458,302	238,116	303,826	45,895	3,061		1,049,200

Total assets	**603,016**	**286,533**	**1,509,390**	**98,039**	**49,700**	**2,546,678**
Customer accounts	**474,263**	**247,705**	**328,952**	**109,776**	**1,227**	**1,161,923**
Loans and advances to banks (net)[12]			**214,693**			
Trading assets[12,13]			**721,366**			
Financial assets designated at fair value[12]			**7,469**			
Financial investments[12]			**211,486**			
Deposits by banks[12]			**144,043**			
Trading liabilities[12,13]			**577,048**			

For footnotes, see page 89.

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Interim Management Report: Business Review (continued)

Analysis by customer group and global business *(continued)*

Profit before tax

	Half-year to 30 June 2007						
Total	Personal Financial Services US$m	Commercial Banking US$m	Global Banking and Markets US$m	Private Banking US$m	Other[5] US$m	Inter-segment elimination [9] US$m	Total 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)[7]	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
Total operating income	24,501	6,536	8,537	1,718	2,606	(1,806)	42,092
Net insurance claims[8]	(3,605)	44	(38)				(3,599)
Net operating income[4]	20,896	6,580	8,499	1,718	2,606	(1,806)	38,493
Loan impairment (charges)/recoveries and other credit risk provisions	(5,928)	(431)	24	(9)	(2)		(6,346)
Net operating income	14,968	6,149	8,523	1,709	2,604	(1,806)	32,147
Total operating expenses	(10,452)	(2,907)	(4,479)	(929)	(1,650)	1,806	(18,611)
Operating profit	4,516	3,242	4,044	780	954		13,536
Share of profit in associates and joint ventures	213	180	114		116		623
Profit before tax	4,729	3,422	4,158	780	1,070		14,159

	%	%	%	%	%	%
Share of HSBC s profibefore 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[6]

	U$Sm	US$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)[12]			183,708			
Trading assets[12,13]			567,340			
Financial assets designated at fair value[12]			5,269			
Financial investments[12]			174,095			
Deposits by banks[12]			121,744			
Trading liabilities[12,13]			443,634			

For footnotes, see page 89.

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Profit before tax

Total	Personal Financial Services US$m	Commercial Banking US$m	Global Banking and Markets US$m	Private Banking US$m	Other[5] US$m	Inter-segment elimination[9] US$m	Total US$m
	Half-year to 31 December 2007						
Net interest income/(expense)	15,071	4,769	2,583	649	(251)	(3,256)	19,565
Net fee income/(expense)	6,219	2,068	2,637	804	(221)		11,507
Trading income excluding net interest income	37	144	455	270	201		1,107
Net interest income/(expense) on trading activities	48	18	(85)	5	(26)	3,256	3,216
Net trading income[7]	85	162	370	275	175	3,256	4,323
Net income/(expense) from financial instruments designated at fair value	537	46	(175)	(1)	2,802		3,209
Gains less losses from financial investments	291	65	545	74	(18)		957
Gains arising from dilution of interests in associates					16		16
Dividend income	14	4	47	2	5		72
Net earned insurance premiums	4,536	528	47		(12)		5,099
Other operating income	132	163	689	27	1,856	(2,106)	761
Total operating income	26,885	7,805	6,743	1,830	4,352	(2,106)	45,509
Net insurance claims[8]	(4,542)	(435)	(32)				(5,009)
Net operating income[4]	22,343	7,370	6,711	1,830	4,352	(2,106)	40,500
Loan impairment charges and other credit risk provisions	(10,244)	(576)	(62)	(5)	(9)		(10,896)
Net operating income	12,099	6,794	6,649	1,825	4,343	(2,106)	29,604
Total operating expenses	(11,305)	(3,345)	(4,879)	(1,096)	(1,912)	2,106	(20,431)
Operating profit	794	3,449	1,770	729	2,431		9,173
Share of profit in associates and joint ventures	377	274	193	2	34		880
Profit before tax	1,171	3,723	1,963	731	2,465		10,053
	%	%	%	%	%		%
Share of HSBC s profit before tax	11.7	37.0	19.5	7.3	24.5		100.0
Cost efficiency ratio	50.6	45.3	72.7	59.9	43.9		50.4

Balance sheet data[6]

	U$Sm	US$m	US$m	US$m	US$m	US$m
Loans and advances to customers (net)	464,726	220,068	250,464	43,612	2,678	981,548
Total assets	588,473	261,893	1,375,240	88,510	40,150	2,354,266
Customer accounts	450,071	237,987	299,879	106,197	2,006	1,096,140
Loans and advances to banks (net)[12]			199,506			
Trading assets[12,13]			625,132			
Financial assets designated at fair value[12]			7,936			
Financial investments[12]			224,057			
Deposits by banks[12]			126,395			
Trading liabilities[12,13]			483,881			

For footnotes, see page 89.

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Geographical regions

Summary

In the analysis of profit and loss by geographical region that follows, operating income and operating expenses include intra-HSBC items of US$1,169 million (first half of 2007: US$852 million; second half of 2007: US$1,133 million).

Profit/(loss) before tax

	Half-year to					
	30 June 2008		30 June 2007		31 December 2007	
	US$m	**%**	US$m	%	US$m	%
Europe	**5,177**	**50.5**	4,050	28.6	4,545	45.2
Hong Kong	**3,073**	**30.0**	3,330	23.5	4,009	39.9
Rest of Asia-Pacific	**3,624**	**35.4**	3,344	23.6	2,665	26.5
North America	**(2,893)**	**(28.2)**	2,435	17.2	(2,344)	(23.3)
Latin America	**1,266**	**12.3**	1,000	7.1	1,178	11.7
	10,247	**100.0**	14,159	100.0	10,053	100.0

Total assets6

	At 30 June 2008		At 30 June 2007		At 31 December 2007	
	US$m	**%**	US$m	%	US$m	%
Europe	**1,313,319**	**51.5**	1,040,019	48.3	1,184,315	50.3
Hong Kong	**325,692**	**12.8**	300,681	14.0	332,691	14.1
Rest of Asia-Pacific	**259,041**	**10.2**	201,123	9.4	228,112	9.7
North America	**531,607**	**20.9**	519,693	24.2	510,092	21.7
Latin America	**117,019**	**4.6**	88,925	4.1	99,056	4.2
	2,546,678	**100.0**	2,150,441	100.0	2,354,266	100.0

Europe

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

	Personal Financial Services US$m	Commercial Banking US$m	Global Banking and Markets[14] US$m	Private Banking US$m	Other US$m	Total US$m
Half-year to 30 June 2008						
UK	**1,164**	**1,656**	**329**	**162**	**168**	**3,479**
France[15]	**122**	**151**	**492**	**14**	**(70)**	**709**
Germany		**21**	**122**	**20**	**(8)**	**155**
Malta	**26**	**33**	**12**			**71**
Switzerland				**335**		**335**
Turkey	**19**	**51**	**56**			**126**
Other	**(7)**	**28**	**179**	**48**	**54**	**302**
	1,324	**1,940**	**1,190**	**579**	**144**	**5,177**
Half-year to 30 June 2007						
UK	384	1,001	902	198	(79)	2,406
France[15]	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
	604	1,236	1,674	493	43	4,050

For footnotes, see page 89.

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	Personal Financial Services US$m	Commercial Banking US$m	Global Banking and Markets[14] US$m	Private Banking US$m	Other US$m	Total US$m
Half-year to 31 December 2007						
UK	837	1,063	312	119	1,055	3,386
France[15]	76	73	231	16	(75)	321
Germany		17	70	20	19	126
Malta	19	32	27			78
Switzerland				215		215
Turkey	73	41	62	(1)		175
Other	(28)	54	151	53	14	244
	977	1,280	853	422	1,013	4,545

Loans and advances to customers (net) by country

	At 30 June 2008 US$m	At 30 June 2007 US$m	At 31 December 2007 US$m
UK	**380,051**	325,199	326,927
France[15]	**78,376**	67,670	81,473
Germany	**7,638**	5,763	6,411
Malta	**4,684**	3,700	4,157
Switzerland	**14,829**	11,164	13,789
Turkey	**8,127**	6,148	7,974
Other	**15,255**	8,464	11,544
	508,960	428,108	452,275

Customer accounts by country

	At 30 June 2008 US$m	At 30 June 2007 US$m	At 31 December 2007 US$m
UK	**413,593**	346,547	367,363
France[15]	**60,281**	48,961	64,905
Germany	**11,054**	9,671	10,282
Malta	**6,292**	4,779	5,947
Switzerland	**42,125**	35,266	41,015
Turkey	**7,090**	5,074	6,473
Other	**9,205**	8,210	8,969

	549,640	458,508	504,954

For footnotes, see page 89.

Economic briefing

The **UK** economy slowed in the first half of 2008. Gross Domestic Product (GDP) increased by 2.0 per cent during the first half of the year against the comparable period of 2007, below the average of the past decade. The housing market deteriorated markedly as the number of mortgage approvals for house purchases fell sharply and nominal house prices recorded small but persistent monthly declines. Employment growth was subdued, with some measures of unemployment increasing slightly during the second quarter of 2008. The Bank of England cut interest rates by 50 basis points during the first half of 2008, although a sharp rise in

inflation to an annual rate of 3.8 per cent in June complicated the outlook for monetary policy during the second half of the year.

Having expanded by 2.6 per cent in 2007, GDP in the **eurozone** rose by 2.1 per cent year-on-year in the first quarter of 2008 driven, in part, by a strong increase in business investment and a further rise in exports. Labour markets remained relatively robust, with the unemployment rate for the region remaining at about 7 per cent. However, consumer spending growth was subdued and most indicators of activity deteriorated as the second quarter progressed. Inflation continued to pick up during the first half of

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Interim Management Report: Business Review (continued)

Profit before tax

	Half-year to		
Europe	**30 June 2008 US$m**	30 June 2007 US$m	31 December 2007 US$m
Net interest income	**4,475**	3,920	3,826
Net fee income	**4,223**	4,144	4,287
Net trading income	**3,649**	3,338	3,605
Net income/(expense) from financial instruments designated at fair value	**(659)**	348	878
Gains less losses from financial investments	**608**	790	536
Dividend income	**20**	161	10
Net earned insurance premiums	**2,286**	1,480	2,530
Other operating income	**1,427**	262	931
Total operating income	**16,029**	14,443	16,603
Net insurance claims incurred and movement in liabilities to policyholders	**(1,388)**	(1,146)	(2,333)
Net operating income before loan impairment charges and other credit risk provisions	**14,641**	13,297	14,270
Loan impairment charges and other credit risk provisions	**(1,272)**	(1,363)	(1,179)
Net operating income	**13,369**	11,934	13,091
Total operating expenses	**(8,193)**	(7,972)	(8,553)
Operating profit	**5,176**	3,962	4,538
Share of profit in associates and joint ventures	**1**	88	7
Profit before tax	**5,177**	4,050	4,545
	%	%	%
Share of HSBC s profit before tax	**50.5**	28.6	45.2
Cost efficiency ratio	**56.0**	60.0	59.9
Period-end staff numbers (full-time equivalent)	**84,457**	80,912	82,166

Balance sheet data[6]

	US$m	US$m	US$m
Loans and advances to customers (net)	**508,960**	428,108	452,275
Loans and advances to banks (net)	**94,795**	79,817	104,527
Trading assets, financial instruments designated at fair value and financial investments[16]	**481,015**	370,193	445,258
Total assets	**1,313,319**	1,040,019	1,184,315
Deposits by banks	**112,081**	86,912	87,491
Customer accounts	**549,640**	458,508	504,954

For footnotes, see page 89.

the year, rising from an annual rate of 3.1 per cent in December 2007 to 4.0 per cent by June 2008. The European Central Bank responded by raising interest rates by 25 basis points in July, taking the repo rate to 4.25 per cent.

In **Turkey**, economic activity accelerated slightly during the early months of 2008, with first quarter GDP growth rising by 6.6 per cent on the comparable period in 2007. Growth is, however, expected to moderate during the remainder of 2008 in response to weakening business and consumer confidence, political uncertainty and rising interest rates. Headline inflation remained under pressure from increases in energy and food prices, rising from 8.4 per cent in December 2007 to 10.6 per cent in June 2008. The Central Bank of the Republic of Turkey revised its medium-term inflation forecasts and, after initially reducing interest rates, tightened policy, raising rates by 50 basis points in both May and June 2008. The current account deficit widened to above 6 per cent of GDP, although HSBC expects continued capital inflows and the high level of interest rates to provide support to the domestic currency.

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Reconciliation of reported and underlying profit before tax

Half-year to 30 June 2008 (1H08) compared with half-year to 30 June 2007 (1H07)

Europe	1H07 as reported US$m	Disposals and dilution gains[1] US$m	Currency translation[2] US$m	1H07 at 1H08 exchange rates US$m	Acquisitions[1] US$m	Underlying change US$m	1H08 as reported US$m	Reported change %	Underlying change %
Net interest income	3,920	(7)	129	4,042	150	283	4,475	14	7
Net fee income	4,144	122	169	4,435	(46)	(166)	4,223	2	(4)
Other income[3]	5,233	(101)	213	5,345	(49)	647	5,943	14	12
Net operating income[4]	13,297	14	511	13,822	55	764	14,641	10	6
Loan impairment charges and other credit risk provisions	(1,363)		(11)	(1,374)		102	(1,272)	7	7
Net operating income	11,934	14	500	12,448	55	866	13,369	12	7
Operating expenses	(7,972)	5	(299)	(8,266)	(17)	90	(8,193)	(3)	1
Operating profit	3,962	19	201	4,182	38	956	5,176	31	23
Income from associates	88		16	104	(12)	(91)	1	(99)	(88)
Profit before tax	4,050	19	217	4,286	26	865	5,177	28	20

For footnotes, see page 89.

Review of business performance

European operations reported a pre-tax profit of US$5.2 billion compared with US$4.1 billion in the first half of 2007, an increase of 28 per cent. On an underlying basis, pre-tax profits increased by 20 per cent. In March 2007, HSBC acquired the remaining 50 per cent interest in HSBC Assurances in France. In October 2007, HSBC disposed of the Hamilton Insurance Company Limited and Hamilton Life Assurance Company Limited in the UK. Underlying net operating income grew by 6 per cent, in contrast with operating expenses, which fell by 1 per cent.

Personal Financial Services delivered the strongest increase in pre-tax profits due to a solid performance in the UK and continued expansion in Turkey. In the UK, growth was driven by lower operating expenses, in part reflecting the absence of the overdraft fee refund charges recognised in the first half of 2007, lower credit impairment charges and a one-off gain on the disposal of MasterCard Inc. (MasterCard) shares. Commercial Banking was strongly ahead of the first half of 2007, as the strength of established businesses in the UK and France was complemented by strong growth in Turkey and other emerging markets. Commercial Banking also benefited from one-off gains on the disposal of the UK merchant acquiring business to a joint venture with Global Payments Inc., together with its share of the disposal gain on the sale of MasterCard shares. Private Banking performed well, as a result of significant inflows of client assets combined with increased foreign exchange trading profits due to volatile markets. Pre-tax profits declined in Global Banking and Markets, driven by write-downs in credit-related trading exposures, which outweighed improvements in Balance Sheet Management and Rates.

In France, HSBC s disposal of seven regional banks was completed on 2 July 2008 and a profit on disposal of US$2.1 billion will be recognised in the second half of 2008.

The following commentary is on an underlying basis.

Personal Financial Services reported a pre-tax profit of US$1.3 billion, an increase of 97 per cent compared with the first half of 2007. In the UK, pre-tax profit growth was driven by a reduction in loan impairment charges, following the enhanced credit controls introduced since 2006, together with lower operating expenses and a one-off gain on the disposal of MasterCard shares. In France, a US$38 million gain on the disposal of four mutual funds was offset by a fall in net interest income, as a contraction of spreads counteracted the benefit of higher balances. In Turkey, revenue growth, driven by increasing volumes on credit cards, deposit accounts and personal loans, outweighed the significant increase in costs incurred to support business growth and higher loan impairment charges as loan balances grew and seasoned.

In the UK, marketing campaigns primarily focused on higher value customers. The highly successful RateMatcher campaign, launched in April 2008, delivered a significant increase in new mortgage business, with balances transferred

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amounting to US$1.3 billion. Additional non-Rate Matcher mortgage business was also written as a result of the campaign. On current accounts, the acquisition of customers to fee-based packaged accounts continued with the One Great Rate campaign launched in February 2008. The Group also continued its focus on Premier, which was re-launched during 2007 in order to provide seamless cross-border banking for affluent customers.

In France, HSBC s disposal of seven regional banks was completed on 2 July 2008. These subsidiaries had been classified as held for sale and, accordingly, their net profits since February 2008 were reported within other operating income rather than in the individual income statement lines. In its core business in France, HSBC increased market share, building on its growing brand awareness. HSBC s Personal Financial Services business in France, going forward, is focused on its core strategic segment of customers with a strong international connectivity. Premier was relaunched in France in the first half of 2008, supported by an extensive media campaign along with customer acquisition initiatives based on direct marketing. As a result, new Premier account openings have increased by more than 70 per cent since the first half of 2007.

In Turkey, HSBC s organic growth strategy concentrated on delivery through branch expansion and new customer acquisition, predominantly led by credit card products. Investment in network expansion continued throughout the first half of 2008, with the opening of 78 new branches, supported by the addition of more than 1,500 staff since June 2007.

Net interest income was in line with the first half of 2007. In the UK, growth in savings balances and increased spreads on current accounts and credit cards were offset by the effect of a planned reduction in personal lending and credit card balances and a reduction in spreads on savings accounts.

HSBC s increased focus on attracting and retaining deposit customers drove a 19 per cent increase in UK savings account balances for both new and existing customers. A number of new savings products launched in the past year, including a cash e-ISA and Online Bonus Saver, contributed to this growth. The resulting increase in net interest income from volume growth was partly offset by tightening spreads, due to competitive pricing and consecutive base rate cuts.

Average current account balances declined by 5 per cent, due to a reduction in the size of individual customer account balances, driven by recent

increases in food and utility costs. Despite this, the focus on high value customer account acquisition continued, with new Premier account openings 18 per cent above the first half of 2007. Current account spreads increased, driven by funding benefits, resulting in a 1 per cent growth in net interest income on current accounts.

Average unsecured lending balances in the UK declined by 10 per cent, reflecting a shift in risk preference and a greater focus on attracting deposit customers. HSBC maintained a cautious approach to unsecured lending, tightening its credit criteria and employing segmentation and risk-based pricing strategies in order to improve the profitability of new business. Spreads increased on unsecured loans as price rises implemented in the second half of 2007 flowed through the portfolio, while the cost of funds was largely fixed.

Credit card balances were 9 per cent lower than in the first half of 2007, falling to US$14.2 billion. This was predominantly due to the sale of certain non-core credit card portfolios between October 2007 and May 2008 and the more conservative approach to lending noted above. The resulting reduction in net interest income was partly offset by the benefit of a re-pricing exercise undertaken during 2007, which resulted in improved yields.

Average mortgage balances were 2 per cent lower than in the first half of 2007, driven by an industry-wide decline in mortgage volumes. Buy-to-let mortgages continue to represent less than 3 per cent of the UK mortgage portfolio, the result of a decision not to write brokered or self-certified mortgages. Despite turbulence in the UK mortgage industry, the market for remortgages remained relatively healthy and, with many lenders unable to compete, HSBC was able to expand its business, launching its mortgage RateMatcher campaign in April 2008. The campaign proved to be a success, generating significant press coverage and inbound call activity and a 38 per cent increase in mortgage applications compared with the first half of 2007. The RateMatcher campaign boosted HSBC s market share of new mortgage business by value from 3 per cent in the first half of 2007 to 6 per cent in the first half of 2008, with a high of 12 per cent achieved in the month of May. The income benefits of the new business generated by the RateMatcher campaign will be seen in the second half of 2008 due to the time lag between loan approval and draw down.

Excluding the regional banks, net interest income in France fell. Growth in deposit and lending volumes from new customers attracted by direct marketing campaigns was more than offset by

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narrower spreads, higher liquidity costs and a lower benefit from net free funds.

In Turkey, net interest income rose by 22 per cent, largely from increased card balances, where HSBC s customer acquisition strategy led to a 37 per cent increase in credit cards in circulation, supported by a larger branch network and several new products, including co-branded and partnership cards. This volume-related growth was partially offset by a narrowing in spreads due to a sharp reduction in the interest rate cap set by the Central Bank of the Republic of Turkey. Competitive pricing designed to gain market share also led to an increase in volumes on deposit accounts and overdrafts, which more than compensated for the resulting decline in margins.

Net fee income was 5 per cent lower as an increase in Turkey offset a decline in France and a fall in the UK, partly due to a reduction in credit card fee income as a result of the partial disposal of the non-core credit card portfolios referred to above. In Turkey, credit card fees increased, driven by a 37 per cent increase in the number of cards in force, as a result of cards being deployed as the principal product to deliver customer acquisition. Excluding the regional banks, fee income in France was lower than in the first half of 2007. Increased sales of fee-based packaged accounts partly compensated for lower stock exchange and mutual fund fees, as poor market conditions deterred private investors.

Net trading income declined by 27 per cent. The movement in trading income largely reflected the fair value measurement of embedded options linked to government regulated home savings products in France.

Net income from financial instruments designated at fair value fell significantly to a loss of US$761 million. This was driven by falling investment markets affecting assets held within the life insurance businesses in France, the UK and Malta. A corresponding movement within net insurance claims and movement in liabilities to policyholders partially offset this decline.

Gains less losses from financial investments increased significantly to US$182 million, driven by a US$38 million gain on the disposal of four mutual funds in France during January 2008 and a US$160 million gain on disposal of MasterCard shares in the UK in June 2008.

Net earned insurance premiums increased by 4 per cent to US$2.1 billion, mainly in the UK due to continued sales of the new Guaranteed Income Bond which was launched in July 2007 and due to

the reclassification of certain pension contracts as insurance rather than investment products following the addition of enhanced life insurance features. In France, net insurance premiums reduced following the ceding of premiums under a significant reinsurance transaction in the first half of 2008. Excluding this, premium income was higher due to the success of promotional offers. The additional premiums led to additional policyholder liabilities being established and therefore to an increase in net insurance claims.

Other operating income increased to US$252 million, compared with an expense of US$110 million in the first half of 2007. This was mainly due to the non-recurrence of the Financial Services Authority (FSA) rule changes implemented in May 2007, which affected the present value of in-force insurance (PVIF) policies in the UK. In France, the reclassification of the regional banks as held for sale resulted in their net profits of US$15.3 million since February 2008 being reported in other operating income.

Loan impairment charges fell by 15 per cent; in the UK, they were 22 per cent below the same period in 2007 due to stable delinquency levels in the core unsecured portfolios and the disposal of selected non-core credit card portfolios referred to above. Mortgage impairment charges in the UK have gradually increased from their historically low levels in line with HSBC s expectations and market conditions. In France, loan impairment charges increased slightly, mainly as a result of a reduction in limits applied to unauthorised overdrafts at the end of 2007 in accordance with new guidelines issued by the Commission Bancaire. Overall, credit quality in France remained good. In Turkey, loan impairment charges rose by 287 per cent, due to increased volumes of credit cards and personal loans, combined with rising delinquency rates. In recognition of this, HSBC tightened its new account underwriting criteria at the start of 2008, with increased cut-off scores, lower credit lines and revised account management policies.

Operating expenses improved by 9 per cent, mainly driven by the non-recurrence of overdraft fee refunds in the UK. There was a reduction in defined benefit pension costs, as a result of an actuarial assessment, and this partly offset an increase in rental charges following the sale and leaseback of UK branch properties. Excluding the regional banks, costs in France decreased, mainly due to a reduction in staff pension and post-retirement healthcare costs following the transfer of certain obligations to a third party. There was an increase in Premier marketing costs as the product was relaunched. Organic

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business expansion in Turkey was supported by a 34 per cent increase in operating expenses as 78 new branches were opened and staff numbers increased by more than 1,500 since June 2007.

Commercial Banking reported pre-tax profits of US$1.9 billion, an increase of 53 per cent compared with the first half of 2007. Revenues were boosted by gains of US$425 million and US$103 million on the sale of the UK merchant acquiring business to a joint venture with Global Payments Inc., as well as a share of the profits on the sale of MasterCard shares, respectively. Excluding these items, profit before tax rose by 11 per cent and revenues by 6 per cent, driven by the continued strength of established businesses in the UK and France augmented by new and growing operations in the developing markets in Turkey and in central and eastern Europe.

Following the roll-out of International Banking Centres and other infrastructure investment in previous years, the volume of cross-border business increased significantly. Successful outward referrals through the Group s Global Links system increased by 122 per cent, including a 138 per cent rise in outward referrals from the UK. The attraction of HSBC s international franchise was illustrated by the Group s capture of a leading share of UK start-ups and business banking customers with an international focus.

In the UK, HSBC continued to focus on enhancing customer experience through the recruitment of sales staff and investment in direct channels in support of a strategic ambition to be recognised as the best bank for small business . In the first half of 2008, more than 100 branch-based business tills were opened and HSBC re-deployed 83 local business managers into key branch sites to provide additional local specialist support for customers located outside major conurbations.

HSBC continued to concentrate investment in the developing markets of central and eastern Europe and in Turkey. New receivables finance businesses were launched in Poland and the Czech Republic and, in Turkey, a further 18 branches were opened providing services to micro, small and mid-market customers. Across central and Eastern Europe, HSBC increased income by 49 per cent.

In France, following HSBC s disposal of seven regional banks which was completed on 2 July 2008, HSBC remains well positioned to benefit from the Group s international presence and is supporting this opportunity by investing in a new development programme, including 10 new Corporate Banking Centres and an expanded product range.

Net interest income rose by 2 per cent, to US$1.7 billion, largely driven by an increase of 43 per cent in Turkey and a more modest rise in the UK.

In the UK, average lending balances increased by 13 per cent. This was broadly based as strong volumes of new business were generated from HSBC s client base, particularly in the mid-market segment. The income benefit from lending volume growth was partly offset by lower spreads as yields fell in the competitive market. However, new lending spreads in the corporate, mid and small business segments increased by 14 basis points and 21 basis points compared with the first and the second halves of 2007, respectively, as market liquidity for new credit reduced, driving prices higher. Net interest income on sterling overdrafts declined as the benefit of a modest increase in average balances was more than offset by tighter spreads. As part of its market positioning to its preferred customer base, HSBC reduced the rate charged to customers for unauthorised overdrafts, further constraining net interest income.

Average current account balances and spreads were broadly in line with the first half of 2007. Average foreign currency denominated current accounts grew, driven by customer acquisition, although the benefit of volume growth was more than offset by lower spreads in the declining US dollar interest rate environment.

HSBC s strong capital position during a period of industry uncertainty helped to attract customer deposits and average deposits increased as a result. The benefit was offset by lower spreads as a reduction in interest rates paid to customers lagged base rate cuts in the first half of 2008.

In Turkey, higher net interest income was driven by growth in both loans and deposits as HSBC expanded across the country. Average loan and trade services balances increased by 15 per cent, following very strong customer acquisition. Micro, small and mid-sized customer numbers rose by 21 per cent in the period driven by branch expansion. The number of branches servicing Commercial Banking customers rose from 89 at 31 December 2007 to 107 at 30 June 2008. Customer acquisition was also boosted by the success of bundled products, including overdrafts, commercial car loans and small and micro business product bundles. The opening of three new Corporate Banking Centres in Istanbul also contributed. The benefits from loan growth were augmented by wider spreads as the proportion of higher yielding small and mid-market lending increased. Average deposit balances also rose, due to

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customer acquisition and competitive pricing, offset by slightly lower spreads from a shift in product mix to higher yielding deposits.

Excluding HSBC s French regional banks, net interest income in France was broadly in line with the first half of 2007 as growth in deposit and lending volumes were offset by narrower spreads, higher liquidity costs and a lower benefit from net free funds. Both average current account balances and deposits increased, driven by customer acquisition and initiatives taken to increase market share in small business banking. Average loan balances rose by 15 per cent as HSBC gained market share. This was partly offset by tighter spreads.

Net fee income increased by 3 per cent to US$1.1 billion. This was largely driven by higher fees in Turkey and the UK, where the rise in volumes in the mid-market segment, noted above, had a corresponding effect on related fee income. Payments and cash management, factoring, trade and insurance products also contributed to the growth in fees in Turkey.

Net fee income in the UK rose by 5 per cent. Higher card issuing fees were driven by an increase in transaction volumes, primarily due to the success of the revolving commercial credit card following its launch in 2006. Currency volatility in the first half of 2008 helped to drive higher transaction volumes and commissions from foreign exchange activity. A decline in lending fees offset these following a reduction in early repayment fees.

In France, excluding the regional banks, net fee income was 8 per cent higher than in the first half of 2007. Volumes rose as a consequence of the client acquisition noted above and increased marketing to existing customers, triggering a strong increase in banking transaction fees. This was offset by lower brokerage and mutual fund fees, as uncertain market conditions subdued investment sentiment and led customers to switch from investment fund products to deposit accounts.

A *net loss from financial instruments designated at fair value* of US$75 million compared with income of US$9 million in the first half of 2007. This fall was largely a result of a decline in value of equity investments held to support liabilities under insurance contracts, mainly offset by the change in net insurance claims and movement in liabilities to policyholders.

The sale of certain mutual funds in France and MasterCard shares in the UK led to an increase in *gains less losses from financial investments*.

As part of the Group s strategy to grow the insurance business, HSBC introduced a new guaranteed investment bond and enhanced the benefits of some existing customer policies, which resulted in higher *net insurance premiums* and a PVIF gain in *other operating income*, respectively. The increase in other operating income was also driven by the gain on sale of the UK merchant acquiring business. Increased net insurance premiums were partly offset by a rise in net insurance claims.

Loan impairment charges of US$285 million were 10 per cent higher than in the first half of 2007, largely due to higher charges in France and Turkey following balance sheet growth. Loan impairment charges in the UK were broadly flat, notwithstanding a 13 per cent growth in lending and a weakening economic environment.

Operating expenses were unchanged from the first half of 2007. In the UK, a focus on efficient delivery of customer service through direct channels allowed investment in additional customer-facing staff in the commercial centres and the commercial wealth business. Additional investment in relationship managers and local business managers helped to improve customer retention and broaden the range of services delivered.

Increased utilisation of direct channels was evidenced by a 28 per cent rise in the number of active business internet banking customers. HSBC continued to develop its straight-through processing capability to enable more customers to buy products online. Business Direct, HSBC s commercial direct banking service, attracted over 33,000 new accounts, of which approximately 75 per cent were opened by new HSBC customers.

Excluding the regional banks, costs in France were moderately lower than in the first half of 2007. This was due to reductions in staff pension and post-retirement healthcare costs following the transfer of certain obligations to external parties, and the beneficial effect of efficiency initiatives, partly offset by the non-recurrence of a litigation provision release.

In Turkey, costs rose by 32 per cent, driven by investment in a larger branch network together with increased marketing costs to support business expansion in the small and micro segments through the enlarged branch network. Staff costs increased by 15 per cent and customer facing staff numbers by 39 per cent as HSBC focused on customer service and product delivery in the expanded network.

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Interim Management Report: Business Review (continued)

Global Banking and Markets profit before tax declined by 34 per cent to US$1.2 billion, primarily due to US$1.4 billion of write-downs in credit-related trading exposures and leveraged and acquisition finance loans, coupled with a reduction in Principal Investments revenues. These more than offset strong profit growth in Balance Sheet Management and Global Banking, and strong performances in the foreign exchange and Rates businesses.

Total operating income fell by 14 per cent to US$3.8 billion. The tighter credit and liquidity conditions in the UK which contributed to the write-downs referred to above were also reflected in a reduction in Principal Investments income after the excellent result in the first half of 2007. Higher revenues in other areas, most notably Rates in the UK and France and Balance Sheet Management in the UK, were driven by greater market volatility. Balance Sheet Management revenues increased by US$384 million in Europe. Global Banking revenues increased by 27 per cent as write-downs on leveraged and acquisition finance loans were more than offset by gains on credit default swap transactions in other parts of the portfolio.

Net interest income rose by 166 per cent, led by strong growth in Balance Sheet Management revenues in the UK due to increased margins driven by steepening sterling and US dollar yield curves. There was also growth in the UK from a focused enlargement of secured lending (repo) business. The UK also benefited from growth in payments and cash management activity, which was driven by a 33 per cent rise in deposits as customers responded to the volatile markets by increasing their cash holdings.

Net fee income declined in the UK and France in Global Markets. Higher cross-selling fees paid to Commercial Banking for generating foreign exchange business reduced net fee income but were more than compensated for by higher trading income on foreign exchange. A decline in equity markets also reduced funds under management in Global Asset Management, further contributing to lower fees.

Trading income fell by 29 per cent, chiefly from the write-downs noted above. As the market turmoil continued, the fair value of asset-backed securities and structured credit instruments further deteriorated as the credit and liquidity disruption that began in the US sub-prime market spread into other mortgage and mortgage-related products. HSBC had mitigated its risk from such events by purchasing protection from monoline insurers against losses from defaults,

primarily on asset-backed credit products. The market turmoil initially caused the fair value of this protection to increase significantly, reflecting the market view that it was more likely that defaults would occur on the underlying asset-backed paper. This sudden increase in the potential liabilities of the monoline insurers resulted in their credit ratings being downgraded as the scale of the liabilities incurred cast significant doubt on the ability of many monoline insurers to pay. Accordingly, a credit risk write-down was taken against the fair value of the exposure to monoline insurers. The market turmoil also caused the market value of some leveraged and acquisition finance loans to fall due to general credit and liquidity disruption. More information on these write-downs and the underlying assets is provided on page 113.

Partially offsetting these trading losses, Rates trading grew by 115 per cent due to high customer demand for inflation protection products in the UK and France. Foreign exchange trading revenues also rose, by 38 per cent, as market volatility continued, and equities grew by 79 per cent, excluding the effect of the gain on the sale of HSBC s investment in Euronext N.V. in 2007. Further income arose from the fair value gains in Global Banking.

A loss of US$218 million was recognised in *net income from financial instruments designated at fair value*. This was due to a loss on euro-denominated debt which is offset in trading income.

Gains less losses from financial investments and *dividend income* both declined in comparison with the very strong performance in the first half of 2007 from the Principal Investments business. In 2008, the number of investments realised fell and the exit multiples achieved were reduced.

The *loan impairment charge* was small and represented only one basis point of customer loans and advances. This compared with a release in the first half of 2007. The UK credit environment for large corporate lending undoubtedly weakened in the first half of 2008, as evidenced by weak retail sales, falling commercial property prices and the restructuring of much of the UK house building sector.

Operating expenses fell by 2 per cent, reflecting lower bonus costs in the UK which were in line with financial performance. This was partly offset by higher administrative expenses in both the UK and France, where IT costs rose due to growth in headcount to support the increased volume and scope of business in Global Markets, including cross-sales and product control.

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Private Banking reported a pre-tax profit of US$579 million, an increase of 15 per cent, compared with the first half of 2007. Good performances were recorded in both Switzerland and Monaco as a result of strong deposit growth, gains on the disposal of the Hermitage Fund and an increase in client foreign exchange trading. However, the cost efficiency ratio worsened by 1.8 percentage points to 54.9 per cent due to higher staff costs caused primarily by the non-recurrence of a pension saving in 2007. Despite this, the cost efficiency ratio remained one of the lowest in the industry.

Net interest income grew by 38 per cent to US$515 million, primarily due to strong deposit growth augmented by widening interest rate spreads in the first half of 2008. In Switzerland and the UK, average customer deposits grew by 35 per cent and 12 per cent to US$42.1 billion and US$15.0 billion, respectively. The growth in deposits was driven by net new money and customers switching from investment securities to cash deposits during the recent market turbulence.

Net fee income increased by 2 per cent to US$559 million, with a 3 per cent increase in funds under management in Switzerland and higher performance fees on UK hedge fund products. This was partially offset by a decline in UK real estate fee income, as expectations of falling house prices drove lower transaction volumes and the non-recurrence of a large tax advisory fee in the first half of 2007. Management fees decreased in France as the private bank exited some business with institutional clients following a decision not to market to this segment and, in Germany, as the market value of funds declined.

Market volatility led to increased foreign exchange trading by clients in Switzerland, contributing to a 28 per cent rise in trading income.

Gains less losses from financial investments were 81 per cent higher at US$78 million. The increase related to the disposal of HSBC s residual holding in the Hermitage Fund, following earlier disposals in 2006 and 2007.

Client assets, which include deposits and funds under management, increased by 2 per cent to US$262.7 billion compared with 31 December 2007. The growth in client assets was driven by US$10.0 billion of net new money, mainly due to client acquisition in Switzerland and Monaco and foreign exchange gains. However, this was partly offset by a decline in the market value of investment securities, particularly equities. The growth in cross-referrals continued, with inward referrals from other customer groups contributing US$1.9 billion to total client assets, an increase of 68 per cent, compared with the first half of 2007.

Operating expenses rose by 23 per cent to US$699 million due to a US$65 million non-recurring pension benefit which occurred in the first half of 2007 and hiring for business growth, which increased property and compensation costs.

Within **Other**, profit before tax rose by 126 per cent to US$144 million, largely due to fair value movements on HSBC s own debt and related derivatives. Widening credit spreads resulted in gains of US$395 million in the first half of 2008 compared to gains of US$6 million in the first half of 2007 and a gain of US$1,254 million in the second half of 2007. These movements will reverse over the remaining life of the debt.

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Interim Management Report: Business Review (continued)

Reconciliation of reported and underlying profit before tax

	Half-year to 30 June 2008 (1H08) compared with half-year to 31 December 2007 (2H07)								
Europe	2H07 as reported US$m	Disposals and dilution gains[1] US$m	Currency translation[2] US$m	2H07 at 1H08 exchange rates US$m	Acquisitions[1] US$m	Underlying change US$m	1H08 as reported US$m	Reported change %	Underlying change %
Net interest income	3,826	(5)	(11)	3,810		665	4,475	17	17
Net fee income	4,287		6	4,293		(70)	4,223	(1)	(2)
Other income[3]	6,157	19	(34)	6,142		(199)	5,943	(3)	(3)
Net operating income[4]	14,270	14	(39)	14,245		396	14,641	3	3
Loan impairment charges and other credit risk provisions	(1,179)		26	(1,153)		(119)	(1,272)	(8)	(10)
Net operating income	13,091	14	(13)	13,092		277	13,369	2	2
Operating expenses	(8,553)	2	(12)	(8,563)		370	(8,193)	4	4
Operating profit	4,538	16	(25)	4,529		647	5,176	14	14
Income from associates	7		1	8		(7)	1	(86)	(88)
Profit before tax	4,545	16	(24)	4,537		640	5,177	14	14

For footnotes, see page 89.

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Analysis by customer group and global business

Profit before tax

Europe	Personal Financial Services US$m	Commercial Banking US$m	Global Banking and Markets US$m	Private Banking US$m	Other US$m	Inter-segment elimination[9] US$m	Total US$m
	Half-year to 30 June 2008						
Net interest income/(expense)	3,373	1,739	1,351	515	(156)	(2,347)	4,475
Net fee income	1,479	1,134	999	559	52		4,223
Trading income excluding net interest income	34	18	1,362	106	33		1,553
Net interest income/(expense) on trading activities	(1)	20	(285)	7	8	2,347	2,096
Net trading income[7]	33	38	1,077	113	41	2,347	3,649
Net income/(expense) from financial instruments designated at fair value	(761)	(75)	(218)		395		(659)
Gains less losses from financial investments	182	140	190	78	18		608
Dividend income	1	2	11	4	2		20
Net earned insurance premiums	2,084	213			(11)		2,286
Other operating income	252	581	362	4	251	(23)	1,427
Total operating income	6,643	3,772	3,772	1,273	592	(23)	16,029
Net insurance claims[8]	(1,290)	(98)					(1,388)
Net operating income[4]	5,353	3,674	3,772	1,273	592	(23)	14,641
Loan impairment (charges)/recoveries and other credit risk provisions	(963)	(285)	(29)	5			(1,272)
Net operating income	4,390	3,389	3,743	1,278	592	(23)	13,369
Total operating expenses	(3,065)	(1,449)	(2,554)	(699)	(449)	23	(8,193)
Operating profit	1,325	1,940	1,189	579	143		5,176
Share of profit/(loss) in associates and joint ventures	(1)		1		1		1
Profit before tax	1,324	1,940	1,190	579	144		5,177
	%	%	%	%	%		%
Share of HSBC s profit before tax	12.9	18.9	11.6	5.7	1.4		50.5
Cost efficiency ratio	57.3	39.4	67.7	54.9	75.8		56.0
Balance sheet data[6]							
	US$m	US$m	US$m	US$m	US$m		US$m
	153,460	111,791	210,727	31,933	1,049		508,960

Loans and advances to customers (net)						
Total assets	**207,810**	**133,372**	**897,664**	**67,408**	**7,065**	**1,313,319**
Customer accounts	**183,608**	**105,135**	**196,432**	**64,242**	**223**	**549,640**
Loans and advances to banks (net)[12]			**78,488**			
Trading assets[12,13]			**482,034**			
Financial instruments designated at fair value[12]			**6,914**			
Financial investments[12]			**88,717**			
Deposits by banks[12]			**105,792**			
Trading liabilities[12,13]			**365,523**			

For footnotes, see page 89.

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H S B C H O L D I N G S P L C

Interim Management Report: Business Review (continued)

Analysis by customer group and global business *(continued)*

Profit before tax

	Half-year to 30 June 2007						
Europe	Personal Financial Services US$m	Commercial Banking US$m	Global Banking and Markets US$m	Private Banking US$m	Other US$m	Inter-segment elimination[9] US$m	Total 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) excluding net interest income	45	11	1,705	83	(2)		1,842
Net interest income/(expense) on trading activities	(2)	12	(268)	4	1	1,749	1,496
Net trading income/(expense)[7]	43	23	1,437	87	(1)	1,749	3,338
Net income/(expense) from financial instruments designated at fair value	315	9	(2)		26		348
Gains less losses from financial investments	19	8	651	42	70		790
Dividend income	1	2	144	5	9		161
Net earned insurance premiums	1,380	109			(9)		1,480
Other operating income/(expense)	(110)	(89)	337	9	147	(32)	262
Total operating income	6,206	2,775	4,170	1,031	293	(32)	14,443
Net insurance claims[8]	(1,245)	99					(1,146)
Net operating income[4]	4,961	2,874	4,170	1,031	293	(32)	13,297
Loan impairment (charges)/recoveries and other credit risk provisions	(1,127)	(256)	17	3			(1,363)
Net operating income	3,834	2,618	4,187	1,034	293	(32)	11,934
Total operating expenses	(3,244)	(1,382)	(2,513)	(541)	(324)	32	(7,972)
Operating profit/(loss)	590	1,236	1,674	493	(31)		3,962
Share of profit in associates and joint ventures	14				74		88
Profit before tax	604	1,236	1,674	493	43		4,050
	%	%	%	%	%		%
Share of HSBC s profit before tax	4.3	8.7	11.8	3.5	0.3		28.6
Cost efficiency ratio	65.4	48.1	60.3	52.5	110.6		60.0

Balance sheet data[6]						
	US$m	US$m	US$m	US$m	US$m	US$m
Loans and advances to customers (net)	149,789	87,247	165,028	25,544	500	428,108
Total assets	198,518	104,420	677,459	56,090	3,532	1,040,019
Customer accounts	166,282	83,421	153,196	54,893	716	458,508
Loans and advances to banks (net)[12]			66,281			
Trading assets[12,13]			354,488			
Financial instruments designated at fair value[12]			3,400			
Financial investments[12]			53,774			
Deposits by banks[12]			85,104			
Trading liabilities[12,13]			265,059			

For footnotes, see page 89.

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	Half-year to 31 December 2007						
Europe	Personal Financial Services US$m	Commercial Banking US$m	Global Banking and Markets US$m	Private Banking US$m	Other US$m	Inter-segment elimination[9] US$m	Total US$m
Net interest income	3,474	1,772	866	428	54	(2,768)	3,826
Net fee income/(expense)	1,632	1,128	1,208	509	(190)		4,287
Trading income excluding net interest income	15	25	952	78	91		1,161
Net interest income/(expense) on trading activities	(5)	18	(342)	5		2,768	2,444
Net trading income[7]	10	43	610	83	91	2,768	3,605
Net income/(expense) from financial instruments designated at fair value	(189)	22	(183)		1,228		878
Gains less losses from financial investments	31	28	449	73	(45)		536
Dividend income		2	11	2	(5)		10
Net earned insurance premiums	2,131	412			(13)		2,530
Other operating income/(expense)	164	54	516	(1)	154	44	931
Total operating income	7,253	3,461	3,477	1,094	1,274	44	16,603
Net insurance claims[8]	(1,969)	(364)					(2,333)
Net operating income[4]	5,284	3,097	3,477	1,094	1,274	44	14,270
Loan impairment (charges)/ recoveries and other credit risk provisions	(917)	(259)	9	(7)	(5)		(1,179)
Net operating income	4,367	2,838	3,486	1,087	1,269	44	13,091
Total operating expenses	(3,391)	(1,559)	(2,637)	(667)	(255)	(44)	(8,553)
Operating profit	976	1,279	849	420	1,014		4,538
Share of profit/(loss) in associates and joint ventures	1	1	4	2	(1)		7
Profit before tax	977	1,280	853	422	1,013		4,545
	%	%	%	%	%		%
Share of HSBC s profit before tax	9.7	12.7	8.5	4.2	10.1		45.2
Cost efficiency ratio	64.2	50.3	75.8	61.0	20.0		59.9
Balance sheet data[6]							
	US$m	US$m	US$m	US$m	US$m		US$m
Loans and advances to customers (net)	151,687	106,846	163,066	30,195	481		452,275
Total assets	200,432	124,464	794,673	60,010	4,736		1,184,315
Customer accounts	178,757	99,704	163,713	62,055	725		504,954
Loans and advances to banks (net)[12]			89,651				

Trading assets[12,13]	396,487
Financial instruments designated at fair value[12]	7,122
Financial investments[12]	94,416
Deposits by banks[12]	85,315
Trading liabilities[12,13]	305,697

For footnotes, see page 89.

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Interim Management Report: Business Review (continued)

Hong Kong

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

	Half-year to		
	30 June 2008 US$m	30 June 2007 US$m	31 December 2007 US$m
Personal Financial Services	**2,036**	1,898	2,314
Commercial Banking	**869**	760	859
Global Banking and Markets	**770**	697	881
Private Banking	**123**	161	144
Other	**(725)**	(186)	(189)
Profit before tax	**3,073**	3,330	4,009

Profit before tax

	Half-year to		
	30 June 2008 US$m	30 June 2007 US$m	31 December 2007 US$m
Net interest income	**2,835**	2,568	2,915
Net fee income	**1,469**	1,439	1,923
Net trading income	**314**	469	773
Net income/(expense) from financial instruments designated at fair value	**(361)**	210	466
Gains less losses from financial investments	**(98)**	32	62
Dividend income	**20**	17	14
Net earned insurance premiums	**1,650**	1,426	1,371
Other operating income	**448**	413	432
Total operating income	**6,277**	6,574	7,956
Net insurance claims incurred and movement in liabilities to policyholders	**(1,169)**	(1,512)	(1,696)
Net operating income before loan impairment charges and other credit risk provisions	**5,108**	5,062	6,260
Loan impairment charges and other credit risk provisions	**(81)**	(80)	(151)
Net operating income	**5,027**	4,982	6,109
Total operating expenses	**(1,975)**	(1,665)	(2,115)
Operating profit	**3,052**	3,317	3,994
Share of profit in associates and joint ventures	**21**	13	15
Profit before tax	**3,073**	3,330	4,009

	%	%	%
Share of HSBC s profit before tax	**30.0**	23.5	39.9
Cost efficiency ratio	**38.7**	32.9	33.8
Period-end staff numbers (full-time equivalent)	**29,467**	27,066	27,655

Balance sheet data[6]

	US$m	US$m	US$m
Loans and advances to customers (net)	**99,741**	89,918	89,638
Loans and advances to banks (net)	**73,461**	68,162	63,737
Trading assets, financial instruments designated at fair value, and financial investments	**78,735**	98,998	102,180
Total assets	**325,692**	300,681	332,691
Deposits by banks	**5,063**	10,383	6,420
Customer accounts	**231,709**	205,219	234,488

For footnote, see page 89.

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Economic briefing

Hong Kong s economy proved robust during the first months of 2008, with year-on-year GDP growth accelerating to 7.1 per cent in the first quarter from 6.9 per cent in the final quarter of 2007. Domestic demand was the major driver of this growth, with both private consumption and fixed asset investment rising sharply. Exports also rose during the first half of 2008, adding further impetus to the economy. Labour markets remained very tight and the unemployment

rate maintained a 10-year low of 3.3 per cent in the second quarter, supporting consumer spending. Investment demand was also strong in the first quarter in the falling interest environment. However, inflation accelerated during the first half of 2008 and while this largely reflected rising food and energy prices, increased rental and wage costs also contributed. The Government s budget measures also supported domestic demand. Interest rates fell in line with US rates.

Reconciliation of reported and underlying profit before tax

	Half-year to 30 June 2008 (1H08) compared with half-year to 30 June 2007 (1H07)								
Hong Kong	**1H07 as reported US$m**	**Disposals and dilution gains[1] US$m**	**Currency translation[2] US$m**	**1H07 at 1H08 exchange rates US$m**	**Acqui-sitions[1] US$m**	**Under-lying change US$m**	**1H08 as reported US$m**	**Re-ported change %**	**Under-lying change %**
Net interest income	**2,568**		**7**	**2,575**		**260**	**2,835**	**10**	**10**
Net fee income	**1,439**		**4**	**1,443**		**26**	**1,469**	**2**	**2**
Other income[3]	**1,055**		**(1)**	**1,054**		**(250)**	**804**	**(24)**	**(24)**
Net operating income[4]	**5,062**		**10**	**5,072**		**36**	**5,108**	**1**	**1**
Loan impairment charges and other credit risk provisions	**(80)**		**(1)**	**(81)**			**(81)**	**(1)**	
Net operating income	**4,982**		**9**	**4,991**		**36**	**5,027**	**1**	**1**
Operating expenses	**(1,665)**		**(4)**	**(1,669)**		**(306)**	**(1,975)**	**(19)**	**(18)**
Operating profit	**3,317**		**5**	**3,322**		**(270)**	**3,052**	**(8)**	**(8)**
Income from associates	**13**			**13**		**8**	**21**	**62**	**62**
Profit before tax	**3,330**		**5**	**3,335**		**(262)**	**3,073**	**(8)**	**(8)**

For footnotes, see page 89.

Review of business performance

HSBC s operations in Hong Kong reported a pre-tax profit of US$3.1 billion, compared with US$3.3 billion in the first half of 2007, a decrease of 8 per cent on both a reported and an underlying basis. The decrease was due to the impairment of certain HSBC strategic investments, which were necessary as a consequence of significant falls in equity market prices. These impairments more than offset profit growth in Personal Financial Services, Commercial Banking and Global Banking and Markets. Underlying net operating income was largely in line with the first half of 2007, while operating expenses grew by 18 per cent, causing a worsening in the cost efficiency ratio to 38.7 per cent.

Pre-tax profits grew in Commercial Banking and Personal Financial Services despite the adverse effects of lower interest rates, driven by strong balance sheet growth through customer acquisition and new product offerings. Strong performance in Global Banking and Markets was driven by

increased income from Balance Sheet Management, as falling interest rates led to a lower cost of funds and a steeper yield curve partially offset by a write-down on an exposure to a monoline insurer. In Private Banking, pre-tax profits fell, largely due to a decline in the value of equities on the Hong Kong stock market, compared with the first half of 2007.

The following commentary is on an underlying basis.

Personal Financial Services reported pre-tax profits of US$2.0 billion, 7 per cent higher than in the first half of 2007. Revenues rose by 7 per cent due to growth in both net interest income and fee income. Higher cost incurred in generating increased business volumes led the cost efficiency ratio to worsen by 1.6 percentage points compared with the first half of 2007 to 29.1 per cent.

Net interest income rose by 6 per cent to US$1.7 billion, driven by deposit volume growth from higher savings balances and by wider margins

Interim Management Report: Business Review (continued)

on most products apart from mortgages, following interest rate cuts.

Average customer deposits were 10 per cent higher than in the first half of 2007. Continued emphasis on Premier helped to increase balances, the number of Premier customers increasing by 7 per cent in the first half of 2008 to over 311,000. Clients raised deposits in response to weaker investment sentiment following falls in local stock markets while, following the launch of campaigns offering preferential time deposit rates and the enhancement of HSBC s Smart Picks platform, HSBC also attracted new deposits. Deposit spreads widened, benefiting from pricing changes made to increase yields.

The property market in Hong Kong remained resilient, buoyed by the low interest rate environment and strong economic fundamentals, though the rate of property transactions and price growth slowed during the period. HSBC selectively reintroduced fixed-rate mortgages, boosting the volume of new mortgages, which rose by 82 per cent. Mortgage offerings to Premier customers continued to be well received, and the proportion of new HSBC home mortgage loans drawn down by Premier customers reached 43 per cent at 30 June 2008. Although yields on new lending increased, strong competition in the residential mortgage market resulted in narrower spreads on the portfolio.

HSBC s leadership in credit cards continued with the launch of the Green Credit Card. A percentage of cardholder spending on this card is directed by the Group to environmental initiatives. This campaign, and a separate acquisition campaign, contributed to the 630,000 new cards issued during the period to bring the total number of cards in circulation to 5.2 million at 30 June 2008. Strong momentum in cardholder spending continued in the first half of the year with an 11 per cent increase. The cards portfolio continued to perform well in the highly competitive environment and is ranked first for market share by multiple measures. Spreads increased due to lower funding costs following declines in market interest rates. This drove a 21 per cent increase in interest income from cards.

Fee income was 8 per cent higher than in the first half of 2007, due to increased sales of investment products and higher income from current account sales, particularly Premier and PowerVantage, a wealth management account package designed for the mid-market customer. Although the volume of transactions on the Hong Kong stock exchange peaked in October 2007, volumes in the first half of

2008 remained above the levels recorded in the same period in 2007.

Income from retail securities and investment products grew by 4 per cent, as customers increasingly utilised online channels to complete transactions. HSBC protected its market share in investment products through programmes and incentives, including preferential brokerage and margin interest offers, and campaigns to sustain awareness of the range of HSBC funds, as well as the promotion of a series of unit trusts that have no subscription fee.

Notwithstanding the launch of new funds in 2007 and the introduction of WealthMaster (a portfolio wealth management sales tool also launched in 2007), funds under management were adversely affected by stock market performance, declining by 9 per cent to US$52 billion, compared with 31 December 2007.

Due to an increased number of cards in circulation and a rise in cardholder balances, credit card fee income rose by 16 per cent.

Though partially offset by lower net claims, income from securities held by the insurance business was adversely affected by the decline in global equity markets. However, *net earned insurance premiums* of US$1.6 billion were 14 per cent higher than in the first half of 2007, driven by increased sales of endowment products in Hang Seng Bank. Of the non-life policies, 81 per cent are now sold through low-cost channels, including the Refundable Protection Plan launched in March through the telesales distribution channel.

Other operating income included a gain of US$159 million from the redemption of shares in the Visa Inc. (Visa) initial public offering (IPO) and the disposal of MasterCard shares.

Credit quality in Hong Kong remained benign, and *loan impairment charges* decreased by 55 per cent, partly as a result of better performance in the cards portfolio. The ratio of non-performing loans to gross advances fell by 7 basis points. Loan impairment charges in the credit card portfolio were lower due to improved delinquency, reflecting bankruptcy trends that were largely in line with the first half of 2007.

Inflation continued to affect wage and premises costs, with *operating expenses* 13 per cent higher. Additional staff were added to frontline roles in the branch network and a programme of branch and self-service banking upgrades was initiated to maintain customer service levels. Marketing costs were largely in line with the first half of 2007,

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notwithstanding new campaigns including the Green Credit Card launch and further emphasis of Premier. IT costs rose in support of business growth and the expansion of self-service banking coverage. Notwithstanding these investments, the cost efficiency ratio remained low, in part due to the use of direct channels. For example, 83 per cent of retail securities transactions were completed online, a 2.9 percentage point improvement.

Commercial Banking recorded a pre-tax profit of US$869 million, 14 per cent higher than in the first half of 2007. Increased revenues were driven by asset and liability growth, along with a rise in fee income from trade and investment products. The credit environment showed mild deterioration; loan impairment charges rose by US$27 million compared with US$1 million in the first half of 2007. The growth in revenue exceeded the growth in costs resulting in a 0.7 percentage point improvement to the cost efficiency ratio.

Customer numbers grew by 8 per cent as HSBC continued to expand its product offerings. 16,000 new Business Vantage accounts were opened during the period, bringing the total to 139,000. HSBC continued successfully to serve the borrowing needs of small businesses through the launch of new products and pre-approved lending offers to existing customers.

Strategic ties with the Hong Kong Trade Development and Productivity Councils were forged to reinforce the small business segment brand and to aid in the acquisition of new lending customers. In addition, HSBC continued to benefit from trade flows between Hong Kong and mainland China, and took various steps to capture cross-border business, leveraging HSBC s customer base and strong presence in the Greater China region. This included the opening of a new centre for small businesses in Sheung Shui in Hong Kong.

Although *net interest income* rose by 6 per cent, strong growth in liability volumes was significantly offset by the effect of narrowing spreads due to lower interest rates.

Net interest income from deposits rose, due to higher deposit balances. Balance growth was due to a series of savings and time deposit campaigns and strong market liquidity. Spreads were lower, as base rates were reduced and market competition remained intense.

Total lending balances rose by 23 per cent, buoyed by customer business activity related to mainland China. Asset spreads contracted during the period, due to significantly lower lending yields than

in 2007 across all customer segments due to lower interest rates and market competition. To encourage further growth in trade finance and factoring, a series of trade promotion programmes was held and a product was launched by Hang Seng Bank to provide customers with a means of benefiting from renminbi appreciation. This contributed to the rise in receivables finance net interest income of 33 per cent compared with the first half of 2007.

HSBC continued to serve a significant number of clients, particularly manufacturers, who received financing to expand their operations in mainland China. Lending to small businesses rose as a result of strong economic growth in Hong Kong. In addition, trade-related lending increased, spurred partly by system enhancements to better capture cross-border business referrals. Trade and supply chain offerings were successful in attracting customers from different segments.

Credit card balances rose by US$22 million, while higher yields caused spreads to increase. The total number of new credit cards in the period reached over 9,400 and there was a 15 per cent increase in income from merchant acquiring compared with the first half of 2007.

Fee income rose by 11 per cent to US$278 million. Trade and supply chain products had strong growth in income and average transaction size. In addition, volumes of remittance transactions and remittance income both rose by 18 per cent. A decline in the sale of interest and foreign exchange linked products, which was partly offset by an increase in demand for equity-linked products, resulted in a fall in overall sales of structured products. The sale of wealth management products to mid-market customers rose, however, and HSBC launched 63 new funds.

Trading income increased by 19 per cent compared with the first half of 2007. Exchange rate volatility continued into the first half of 2008 and the level of trading between US and Hong Kong dollars rose.

Net earned insurance premiums rose by 53 per cent, driven by life products. The composite sales teams introduced in 2007 and the launch in June 2008 of a corporate wealth management branding campaign were used to enhance customer awareness of investment, key person and group medical insurance products.

Loan impairment charges of US$28 million were recorded, an increase from previously low levels. The credit environment proved more volatile than in the first half of 2007, particularly for small

and medium businesses with operations in mainland China. Impaired customer loans were 0.52 per cent of total loans and advances at 30 June 2008, a further 17 basis point improvement on its previously low level.

Operating expenses rose by 13 per cent, due to a combination of higher staff numbers, wage inflation and increased premises costs. Nearly 200 frontline staff were added since 30 June 2007, to provide additional capacity for business growth. IT costs rose as the number of IT-related projects, including the upgrade of internet systems, increased. The number of transactions through direct channels rose to 42 per cent of the total volume. 200,000 customers were registered as internet users at 30 June 2008, compared with 176,000 at the end of 2007. Call centres were also increasingly utilised to generate lower cost sales.

Global Banking and Markets reported a pre-tax profit of US$770 million, an increase of 10 per cent over the first half of 2007. This growth was mainly due to an increase in net interest income in Balance Sheet Management, partly offset by a decline in trading income, driven by a write-down on an exposure to a monoline insurer.

Total operating income rose by 13 per cent to US$1.3 billion. The fall in short-term US and Hong Kong dollar interest rates supported the strong results of Balance Sheet Management and Rates trading. Income from foreign exchange trading benefited from exchange rate volatility. The securities services business earned increased fees, principally in funds services. Partly offsetting this was a monoline exposure write-down in structured credit of US$0.2 billion.

Net interest income grew by 91 per cent to US$801 million, driven mainly by Balance Sheet Management, which increased by US$389 million due to a steepening of the US dollar and Hong Kong dollar yield curves. Net interest income from Global Banking increased by 13 per cent due to an improvement in lending spreads in a more conservative lending environment.

Net fee income decreased, mainly due to higher customer referral fees paid in respect of increased sales of equity-linked investments to retail banking customers; these sales drove a corresponding rise in trading income. Net fee income also decreased due to a decline in initial public offering (IPO) success fees. This was partly offset by a rise in securities services revenues, particularly in funds services. Increased activity by fund managers and greater than expected cash balances contributed to this revenue growth. Higher fees in Global Asset Management

were driven by a number of successful product launches which contributed to US$4.2 billion net new money.

Trading income declined by 43 per cent to US$217 million, due to a write-down in a monoline exposure. For a description of the background to monoline write-downs, see page 36. Performance in Credit also weakened as spreads widened. These declines were mitigated in part by a 72 per cent growth in foreign exchange trading revenues, which were driven by volatile currency markets, increased investment flows and a greater focus on cross-sales to other customer groups. Equities increased by 39 per cent as a result of higher issuance of equity- linked products, in response to market demand from retail customers. Rates income grew by 28 per cent as market conditions drove clients to hedge interest rate risk exposure.

Operating expenses rose by 13 per cent, mainly due to an increase in performance costs resulting from improved revenues in certain businesses, and a rise in staff numbers to support the growth of product areas such as structured equities, securities services and corporate lending. IT costs increased, mainly due to systems development associated with the growth of the Global Markets.

Private Banking reported a pre-tax profit of US$123 million, a decrease of 24 per cent on the first half of 2007. With the decline in the value of equities on the Hong Kong stock market in the first half of 2008, demand for equity-linked structured products diminished, resulting in lower revenue than the strong results in 2007. The cost efficiency ratio worsened by 10.4 percentage points to 50.8 per cent.

Net interest income grew by 96 per cent to US$96 million, with a 33 per cent increase in customer deposits. The growth in customer deposits was driven by customers switching from investment securities to cash deposits, due to market turbulence and poor equity market performance.

Fee income rose by 19 per cent to US$95 million, owing largely to performance fees related to Asian discretionary portfolios and growth of the trust business. Partially offsetting this were lower fees from mutual funds, as funds under management decreased.

Trading income fell by 56 per cent to US$57 million, attributable to the downturn in the Hong Kong stock market. In particular, there was a decline in demand for equity-linked structured products, which were the primary driver of trading income in 2007.

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Client assets decreased by 9 per cent to US$66.4 billion, compared with 31 December 2007 because of the lower market values of funds. Despite this, the growth in cross-referrals continued, with inward referrals from other customer groups contributing US$613 million to total client assets compared with US$190 million the first half of 2007.

Operating expenses increased by 17 per cent to US$127 million, primarily due to a rise in staff costs, which were driven by increased salaries in a competitive labour market and higher numbers of staff recruited in response to a greater number of clients.

Within **Other**, a loss of US$725 million was reported, compared with a loss of US$186 million in the first half of 2007. The decrease was driven by equity market declines, which resulted in total impairments of US$296 million in the value of several of HSBC s strategic investments in the region.

The fall in net interest income was partly due to lower yields on core liquidity partly as a result of a switch to shorter maturities for these investments. Hong Kong head office and central IT costs rose by 22 per cent, reflecting increased activity in supporting business expansion. These costs were substantially offset by recoveries from Group entities.

Reconciliation of reported and underlying profit before tax

	Half-year to 30 June 2008 (1H08) compared with half-year to 31 December 2007 (2H07)								
Hong Kong	2 H07 as reported US$m	Disposals and dilution gains[1] US$m	Currency translation[2] US$m	2 H07 at 1 H08 exchange rates US$m	Acqui-sitions[1] US$m	Under-lying change US$m	1 H08 as reported US$m	Re-ported change %	Under-lying change %
Net interest income	2,915		(2)	2,913		(78)	2,835	(3)	(3)
Net fee income	1,923		(1)	1,922		(453)	1,469	(24)	(24)
Other income[3]	1,422		(2)	1,420		(616)	804	(43)	(43)
Net operating income[4]	6,260		(5)	6,255		(1,147)	5,108	(18)	(18)
Loan impairment charges and other credit risk provisions	(151)			(151)		70	(81)	46	46
Net operating income	6,109		(5)	6,104		(1,077)	5,027	(18)	(18)
Operating expenses	(2,115)		3	(2,112)		137	(1,975)	7	6
Operating profit	3,994		(2)	3,992		(940)	3,052	(24)	(24)
Income from associates	15			15		6	21	40	40
Profit before tax	4,009		(2)	4,007		(934)	3,073	(23)	(23)

For footnotes, see page 89.

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

	Half-year to 30 June 2008						
Hong Kong	**Personal Financial Services US$m**	**Commercial Banking US$m**	**Global Banking and Markets US$m**	**Private Banking US$m**	**Other US$m**	**Inter-segment elimination[9] US$m**	**Total US$m**
Net interest income/(expense)	1,693	770	801	96	(514)	(11)	2,835
Net fee income	856	278	238	95	2		1,469
Trading income/(expense) excluding net interest income	90	37	40	57	(121)		103
Net interest income on trading activities	6	1	177		16	11	211
Net trading income/(expense)[7]	96	38	217	57	(105)	11	314
Net income/(expense) from financial instruments designated at fair value	(455)	15	8		71		(361)
Gains less losses from financial investments	159	34	12		(303)		(98)
Dividend income	2	1	3		14		20
Net earned insurance premiums	1,559	84	6		1		1,650
Other operating income	110	17	47	2	448	(176)	448
Total operating income/(expense)	4,020	1,237	1,332	250	(386)	(176)	6,277
Net insurance claims[8]	(1,104)	(61)	(4)				(1,169)
Net operating income/(expense)[4]	2,916	1,176	1,328	250	(386)	(176)	5,108
Loan impairment (charges)/recoveries and other credit risk provisions	(34)	(28)	(20)		1		(81)
Net operating income/(expense)	2,882	1,148	1,308	250	(385)	(176)	5,027
Total operating expenses	(848)	(279)	(538)	(127)	(359)	176	(1,975)
Operating profit/(loss)	2,034	869	770	123	(744)		3,052
Share of profit in associates and joint ventures	2				19		21
Profit/(loss) before tax	2,036	869	770	123	(725)		3,073

	%	%	%	%	%	%
Share of HSBC s profit before tax	**19.9**	**8.5**	**7.5**	**1.2**	**(7.1)**	**30.0**
Cost efficiency ratio	**29.1**	**23.7**	**40.5**	**50.8**	**(93.0)**	**38.7**

Balance sheet data[6]

	US$m	US$m	US$m	US$m	US$m	US$m
Loans and advances to customers (net)	**40,608**	**32,112**	**20,257**	**4,912**	**1,852**	**99,741**
Total assets	**74,967**	**41,800**	**162,571**	**15,072**	**31,282**	**325,692**
Customer accounts	**133,454**	**49,700**	**31,577**	**16,602**	**376**	**231,709**
Loans and advances to banks (net)[12]			**64,186**			
Trading assets[12,13]			**28,334**			
Financial instruments designated at fair value[12]			**422**			
Financial investments[12]			**34,455**			
Deposits by banks[12]			**4,417**			
Trading liabilities[12,13]			**25,895**			

For footnotes, see page 89.

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Profit/(loss) before tax

	Half-year to 30 June 2007						
Hong Kong	Personal Financial Services US$m	Commercial Banking US$m	Global Banking and Markets US$m	Private Banking US$m	Other US$m	Inter-segment elimination[9] US$m	Total 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) excluding net interest income	74	32	302	130	(13)		525
Net interest income on trading activities	2		80		21	(159)	(56)
Net trading income[7]	76	32	382	130	8	(159)	469
Net income/(expense) from financial instruments designated at fair value	273	(36)	1		(28)		210
Gains less losses from financial 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
Total operating income	4,192	1,040	1,181	270	43	(152)	6,574
Net insurance claims[8]	(1,473)	(34)	(5)				(1,512)
Net operating income[4]	2,719	1,006	1,176	270	43	(152)	5,062
Loan impairment charges and other credit risk provisions	(74)	(1)	(5)				(80)
Net operating income	2,645	1,005	1,171	270	43	(152)	4,982
Total operating expenses	(750)	(246)	(474)	(109)	(238)	152	(1,665)
Operating profit/(loss)	1,895	759	697	161	(195)		3,317
Share of profit in associates and joint ventures	3	1			9		13
Profit/(loss) before tax	1,898	760	697	161	(186)		3,330
	%	%	%	%	%		%
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[6]

	US$m	US$m	US$m	US$m	US$m		US$m
	39,375	25,105	19,231	4,309	1,898		89,918

Loans and advances to customers (net)							
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)[12]			61,850				
Trading assets[12,13]			29,224				
Financial instruments designated at fair value[12]			691				
Financial investments[12]			50,099				
Deposits by banks[12]			9,991				
Trading liabilities[12,13]			24,045				

For footnotes, see page 89.

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Analysis by customer group and global business *(continued)*

Profit/(loss) before tax

	Half-year to 31 December 2007						
Hong Kong	Personal Financial Services US$m	Commercial Banking US$m	Global Banking and Markets US$m	Private Banking US$m	Other US$m	Inter-segment elimination[9] US$m	Total US$m
Net interest income/(expense)	1,754	814	568	21	(395)	153	2,915
Net fee income	1,182	276	364	99	2		1,923
Trading income excluding net interest income	114	31	251	150	199		745
Net interest income on trading activities	3		161		17	(153)	28
Net trading income[7]	117	31	412	150	216	(153)	773
Net income/(expense) from financial instruments designated at fair value	547	23	6		(110)		466
Gains less losses from financial investments			37		25		62
Dividend income	1	1	5		7		14
Net earned insurance premiums	1,288	75	8				1,371
Other operating income/(expense)	56	15	59	(4)	491	(185)	432
Total operating income	4,945	1,235	1,459	266	236	(185)	7,956
Net insurance claims[8]	(1,643)	(48)	(5)				(1,696)
Net operating income[4]	3,302	1,187	1,454	266	236	(185)	6,260
Loan impairment charges and other credit risk provisions	(101)	(27)	(23)				(151)
Net operating income	3,201	1,160	1,431	266	236	(185)	6,109
Total operating expenses	(889)	(301)	(551)	(122)	(437)	185	(2,115)
Operating profit/(loss)	2,312	859	880	144	(201)		3,994
Share of profit in associates and joint ventures	2		1		12		15
Profit/(loss) before tax	2,314	859	881	144	(189)		4,009

	%	%	%	%	%	%
Share of HSBC s profit before tax	23.0	8.5	8.8	1.4	(1.9)	39.9
Cost efficiency ratio	26.9	25.4	37.9	45.9	185.2	33.8

Balance sheet data[6]

	US$m	US$m	US$m	US$m	US$m	US$m
Loans and advances to customers (net)	38,197	25,890	19,171	4,329	2,051	89,638
Total assets	72,386	35,366	185,933	14,138	24,868	332,691
Customer accounts	129,159	51,562	37,364	15,649	754	234,488
Loans and advances to banks (net)[12]			53,725			
Trading assets[12,13]			38,369			
Financial instruments designated at fair value[12]			546			
Financial investments[12]			46,765			
Deposits by banks[12]			6,251			
Trading liabilities[12,13]			26,804			

For footnotes, see page 89.

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Rest of Asia-Pacific (including the Middle East)

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

	Personal Financial Services US$m	Commercial Banking US$m	Global Banking and Markets US$m	Private Banking US$m	Other US$m	Total US$m
Half-year to 30 June 2008						
Australia	**15**	**34**	**47**		**4**	**100**
India	**(53)**	**75**	**301**	**2**	**46**	**371**
Indonesia	**(1)**	**19**	**52**		**(4)**	**66**
Japan	**(39)**		**42**	**1**		**4**
Mainland China	**277**	**306**	**357**	**(2)**	**(31)**	**907**
Associates	**321**	**268**	**159**			**748**
Other mainland China	**(44)**	**38**	**198**	**(2)**	**(31)**	**159**
Malaysia	**61**	**51**	**94**		**3**	**209**
Middle East	**209**	**308**	**426**	**2**	**45**	**990**
Egypt	**11**	**37**	**45**		**22**	**115**
United Arab Emirates	**106**	**184**	**229**	**2**	**1**	**522**
Other Middle East	**44**	**69**	**65**			**178**
Middle East (excluding Saudi Arabia)	**161**	**290**	**339**	**2**	**23**	**815**
Saudi Arabia	**48**	**18**	**87**		**22**	**175**
Singapore	**63**	**45**	**185**	**51**	**(4)**	**340**
South Korea	**(10)**	**(2)**	**168**		**21**	**177**
Taiwan	**(5)**	**12**	**106**		**2**	**115**
Other	**18**	**113**	**194**		**20**	**345**
	535	**961**	**1,972**	**54**	**102**	**3,624**
Half-year to 30 June 2007						
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
Associates	171	147	67		1,078	1,463
Other mainland China	(3)	24	59		6	86
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
	351	597	1,098	56	1,242	3,344

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

	Personal Financial Services US$m	Commercial Banking US$m	Global Banking and Markets US$m	Private Banking US$m	Other US$m	Total US$m
Half-year to 31 December 2007						
Australia	22	21	26		4	73
India	(57)	39	218	(1)	31	230
Indonesia	(9)	14	40		1	46
Japan	(26)	(2)	49	(1)	5	25
Mainland China	326	226	243		17	812
Associates	345	204	153		15	717
Other mainland China	(19)	22	90		2	95
Malaysia	41	62	76	(1)	7	185
Middle East	120	262	279	2	38	701
Egypt	3	24	41		13	81
United Arab Emirates	46	123	149	2	2	322
Other Middle East	46	60	63		3	172
Middle East (excluding Saudi Arabia)	95	207	253	2	18	575
Saudi Arabia	25	55	26		20	126
Singapore	51	52	135	39	6	283
South Korea	(29)	(12)	93		13	65
Taiwan	(17)	14	80		3	80
Other	(13)	77	127	(2)	(24)	165
	409	753	1,366	36	101	2,665

Loans and advances to customers (net) by country

	At 30 June 2008 US$m	At 30 June 2007 US$m	At 31 December 2007 US$m
Australia	**12,664**	9,845	11,339
India	**7,585**	6,216	7,220
Indonesia	**1,924**	1,296	1,642
Japan	**4,710**	3,580	4,258
Mainland China	**12,653**	6,787	11,647
Malaysia	**9,295**	8,003	8,856
Middle East (excluding Saudi Arabia)	**25,004**	17,047	21,607
Egypt	**2,265**	1,196	1,853
United Arab Emirates	**16,416**	10,928	14,103
Other Middle East	**6,323**	4,923	5,651
Singapore	**13,724**	10,768	11,505
South Korea	**6,581**	6,458	7,124

Taiwan	**5,330**	3,834	3,658
Other	**14,287**	14,340	12,996
	113,757	88,174	101,852

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Customer accounts by country

	At 30 June 2008 US$m	At 30 June 2007 US$m	At 31 December 2007 US$m
Australia	**13,864**	10,345	11,418
India	**11,365**	8,827	12,021
Indonesia	**2,557**	2,082	2,574
Japan	**4,728**	3,944	4,657
Mainland China	**18,205**	9,229	14,537
Malaysia	**12,836**	10,629	11,701
Middle East (excluding Saudi Arabia)	**36,256**	26,277	30,937
Egypt	**5,359**	3,358	4,056
United Arab Emirates	**20,658**	15,362	18,455
Other Middle East	**10,239**	7,557	8,426
Singapore	**32,784**	25,885	28,962
South Korea	**4,509**	4,705	5,760
Taiwan	**12,227**	9,208	9,426
Other	**17,464**	16,328	18,240
	166,795	127,459	150,233

Economic briefing

Mainland China maintained a robust level of growth during the first half of 2008, although some mild deceleration was evident as the year-on-year rate of GDP growth slowed from 11.3 per cent in the final quarter of 2007 to 10.1 per cent in the second quarter of 2008. This reflected both a slowing of overseas demand for Chinese exports and the effect of unusual weather patterns and natural disaster. Consumer spending continued to advance at a rapid pace with retail spending increasing by 23 per cent over the year to June 2008, reflecting strong income growth and, in part, rising inflationary pressures. The annual rate of consumer price inflation rose to 7.1 per cent in June 2008, mainly due to higher food prices. Intense price pressures led to a further tightening of economic policy during the first half of 2008. The renminbi continued its gradual appreciation against the US dollar, rising at a slightly higher rate than that of recent years.

Japan s economy, the largest in the region, proved unexpectedly strong during the first quarter of 2008 with GDP rising by 1.3 per cent year-on-year, driven in large part by a rebound in household expenditure and strong external demand. However, most indicators of growth deteriorated during the second quarter of the year. The annual rate of industrial production growth slowed to just 0.2 per cent in June 2008, household expenditure remained subdued and business confidence deteriorated during the second quarter. Inflationary pressures increased during 2008 and the headline rate of consumer price inflation hit a ten-year high of 2.0 per cent in June 2008.

The economies of the **Middle East** continued to perform strongly during the first half of 2008, although inflationary pressures grew as the year progressed. Sharply higher oil prices once again proved the catalyst for expansion, facilitating continued growth in public and private investment. Consumption rose as employment levels increased and low interest rates supported an ongoing expansion in credit. High oil revenues continued to boost fiscal and current account surpluses throughout the Middle East, supporting in turn increases in the holdings of foreign assets.

Elsewhere in Asia, most economies continued to perform reasonably strongly in the first half of 2008, although growing concerns arising from the inflationary outlook prompted a number of central banks across the region to tighten their policies. The Indian economy proved resilient, helped by the strength of activity within the service sector and a sharp rise in government investment expenditure. A sustained rise in inflation during the first half of 2008 prompted the Reserve Bank of India to tighten policy. Economic activity in Singapore was uneven during the first half of the year, with volatility in certain specific industrial sectors. Overall, high levels of loan demand boosted strong growth during the first quarter before activity slowed. The annual rate of inflation continued to advance, hitting a 26-year high of 7.5 per cent in June 2008. Inflation was also the predominant concern in Vietnam as the annual rate of consumer price inflation doubled to 27 per cent during the first half of 2008, prompting the State Bank of Vietnam to sanction substantial interest rate increases. The external trade position

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Interim Management Report: Business Review (continued)

Profit before tax

	Half-year to		
Rest of Asia-Pacific (including the Middle East)	**30 June 2008 US$m**	30 June 2007 US$m	31 December 2007 US$m
Net interest income	**2,633**	1,901	2,242
Net fee income	**1,338**	1,010	1,236
Net trading income	**1,329**	797	846
Net income/(expense) from financial instruments designated at fair value	**(88)**	78	33
Gains less losses from financial investments	**33**	26	12
Gains arising from dilution of interests in associates		1,076	5
Dividend income	**2**	4	4
Net earned insurance premiums	**114**	109	117
Other operating income	**484**	360	438
Total operating income	**5,845**	5,361	4,933
Net insurance claims incurred and movement in liabilities to policyholders	**(4)**	(141)	(112)
Net operating income before loan impairment charges and other credit risk provisions	**5,841**	5,220	4,821
Loan impairment charges and other credit risk provisions	**(369)**	(308)	(308)
Net operating income	**5,472**	4,912	4,513
Total operating expenses	**(2,784)**	(2,075)	(2,689)
Operating profit	**2,688**	2,837	1,824
Share of profit in associates and joint ventures	**936**	507	841
Profit before tax	**3,624**	3,344	2,665
	%	%	%
Share of HSBC s profit before tax	**35.4**	23.6	26.5
Cost efficiency ratio	**47.7**	39.8	55.8
Period-end staff numbers (full-time equivalent)	**93,747**	81,031	88,573

Balance sheet data[6]

	US$m	US$m	US$m
Loans and advances to customers (net)	**113,757**	88,174	101,852
Loans and advances to banks (net)	**51,739**	34,678	39,861
Trading assets, financial instruments designated at fair value, and financial investments	**68,132**	52,189	64,381
Total assets	**259,041**	201,123	228,112
Deposits by banks	**20,539**	13,709	17,560
Customer accounts	**166,795**	127,459	150,233

For footnotes, see page 89.

deteriorated considerably, raising concerns over the sustainability of the currency. First quarter growth in year-on-year terms remained at about 7 per cent in Malaysia, driven by rising food and energy exports. In Indonesia, further strong growth in the first quarter of the year was driven by robust business investment expenditure. However, rising inflationary pressures eventually led Bank Indonesia into a modest tightening of policy. South Korea s economy suffered from its position as one of the most energy intensive economies of the region, with both the

outlook for growth and inflation deteriorating during the first half of 2008. Rising food prices proved particularly problematic for the Philippines economy, with inflation moving well above the central bank s targeted range. Export growth in Taiwan was generally resilient in the face of deteriorating conditions overseas, while robust economic performance in Thailand and Pakistan in the first half of 2008 was overshadowed to varying degrees by lingering domestic uncertainty.

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Reconciliation of reported and underlying profit before tax

Half-year to 30 June 2008 (1H08) compared with half-year to 30 June 2007 (1H07)

Rest of Asia-Pacific (including the Middle East)	1H07 as reported	Disposals and dilution gains1	Currency translation2	1H07 at 1H08 exchange rates	Acqui-sitions1	Under-lying change	1H08 as reported	Re-ported change	Under-lying change
	US$m	US$m	US$m	US$m	US$m	US$m	US$m	%	%
Net interest income	1,901		95	1,996	8	629	2,633	39	32
Net fee income	1,010		50	1,060	1	277	1,338	32	26
Other income[3]	2,309	(1,076)	108	1,341	4	525	1,870	(19)	39
Net operating income[4]	5,220	(1,076)	253	4,397	13	1,431	5,841	12	33
Loan impairment charges and other credit risk provisions	(308)		(12)	(320)		(49)	(369)	(20)	(15)
Net operating income	4,912	(1,076)	241	4,077	13	1,382	5,472	11	34
Operating expenses	(2,075)		(116)	(2,191)	(11)	(582)	(2,784)	(34)	(27)
Operating profit	2,837	(1,076)	125	1,886	2	800	2,688	(5)	42
Income from associates	507		32	539		397	936	85	74
Profit before tax	3,344	(1,076)	157	2,425	2	1,197	3,624	8	49

For footnotes, see page 89.

Review of business performance

Operations in the Rest of Asia-Pacific region reported a pre-tax profit of US$3.6 billion compared with US$3.3 billion in the first half of 2007, an increase of 8 per cent. In the first half of 2007, HSBC recognised non-recurring gains of US$1.1 billion following share offerings made by HSBC s associates Ping An Insurance, Bank of Communications and Industrial Bank. Excluding these dilution gains, profit before tax increased by 49 per cent on an underlying basis.

In the first half of 2008, HSBC acquired the assets, liabilities and operations of The Chinese Bank in Taiwan, increasing the branch network there from eight to 44 and providing a presence in all major cities in Asia s fourth biggest banking market.

Global Banking and Markets performed well, notably in the Middle East, mainland China and South Korea, driven by strong revenue growth from Balance Sheet Management, foreign exchange trading and securities services. Increased profit before tax in Commercial Banking was largely volume driven following customer acquisition, particularly in the mid-market and small business segments. In Personal Financial Services, higher contributions from HSBC associates and increased revenues from personal lending were largely offset by larger loan impairment charges, particularly in India following portfolio growth and increased delinquencies, and investment in business expansion. Pre-tax profits were broadly in line with the first half of 2007 in Private Banking as strong revenue only

partially funded costs associated with expansion in Japan and mainland China.

The following commentary is on an underlying basis and excludes dilution gains.

Pre-tax profits in **Personal Financial Services** were US$535 million, 42 per cent higher than in the first half of 2007. Operating income and the contribution from HSBC s associates increased by 23 per cent and 79 per cent, respectively. Revenue growth across the region was driven by increased fee income and net interest income, with the latter predominantly attributable to the growth of personal lending. Loan impairment charges increased, partly as a result of the deteriorating credit environment and the effects of higher food and energy prices on consumers in India. Notwithstanding significant investment in the key markets of mainland China, the Middle East, India and Japan, the cost efficiency ratio remained in line with the first half of 2007.

Key initiatives in the region included an increased emphasis on offerings to Premier customers and growth of the wealth management business. The number of Premier customers increased by 23 per cent compared with 31 December 2007. Growth was particularly strong in the United Arab Emirates (UAE), India, Singapore, Australia and mainland China, assisted by the expansion of renminbi-denominated services following local incorporation in 2007. In the Middle East, several HSBC One World products for nonresidents were introduced to increase cross-border business.

Interim Management Report: Business Review (continued)

Branches were added during the last 12 months in mainland China, Indonesia, Pakistan, Japan, Sri Lanka and Jordan. Including 32 Hang Seng Bank outlets in Mainland China, the total number of branches in the region was 462, a 24 per cent rise from 30 June 2007. In mainland China, HSBC added 8 new outlets in the period, maintaining its leading position among foreign banks for own-branded branches. Operating expenses rose to support expansion, including more than 1,100 additional staff. HSBC now has over 10,000 frontline staff across the region.

Pre-tax profits rose by 52 per cent in mainland China, with a significant rise in revenues from the locally incorporated bank along with profits from associates which nearly doubled. Net interest income grew strongly, benefiting from substantial volume growth of mortgages and renminbi deposits following branch expansion into the important economic zones of the Pearl River Delta, the Yangtze River Delta and the Bohai Rim. Business expansion was curtailed slightly due to regulatory restrictions on lending growth for banks operating in mainland China, which took effect from the second half of 2007. Fees related to products offered through the Qualified Domestic Institutional Investors (QDII) scheme contributed to a doubling of net fee income.

The Middle East reported profit before tax of US$209 million, an increase of 65 per cent. Revenues rose by 52 per cent, driven by higher net interest income from balance sheet growth and wider spreads in a falling interest rate environment, particularly for personal loans, cards and mortgages. Mortgage balances more than doubled in the UAE, with growth driven by customer demand. Fee income also rose as a result of strong sales of investment and insurance products and higher fees from cards, as both cards in force and cardholder spending increased. New structured products and mutual funds were introduced to match client appetite in the volatile stock market conditions. Trading income rose due to stronger than anticipated foreign exchange income, in part due to higher volatility fuelled by expectations that currencies in the region may be unpegged from the US dollar or revalued.

In Singapore, pre-tax profits grew by 17 per cent, largely attributable to higher net interest income from an increase in deposit balances. Fees rose strongly due to higher sales of investment products and the growth of the credit card business.

In India, a pre-tax loss of US$53 million was recorded, compared with a loss of US$13 million in

the first half of 2007. Investment in the business continued and drove higher asset balances and income growth. Loan impairment charges increased by 181 per cent, driven by volume growth in an adverse credit and collections environment as a result of high interest rates and inflation which inhibited customer repayment capabilities. Operating expenses increased due to higher business volumes and a rise in staff costs combined with a rise in fees paid to collection agencies.

A pre-tax loss in Taiwan was significantly lower than in the first half of 2007, due to reduced loan impairment charges.

Profit before tax in Malaysia rose by 42 per cent following strong revenue growth as a result of higher deposit balances and a rise in card and mortgage balances. In addition, there were gains from the redemption of Visa shares and sale of MasterCard shares. Growth was moderated by reduced consumer interest in investment products and competition in the mortgage sector which resulted in lower spreads.

Net interest income increased by 20 per cent to US$1.2 billion, driven mainly by wider spreads on credit cards and personal lending. Income was substantially higher in the Middle East, India, Indonesia and mainland China. Higher pricing resulted in a widening of asset spreads.

A 14 per cent increase in average deposit balances was largely driven by mainland China and Singapore. The success of Premier was also instrumental in deposit growth in mainland China and India. HSBC Direct balances rose by 58 per cent. Spreads contracted during the period due to falling interest rates.

The mortgage portfolio grew by 9 per cent, excluding New Zealand, where there had been the sale of a mortgage portfolio in the second half of 2007. Growth was recorded in the UAE, Singapore, Australia and mainland China. Mortgage spreads improved, due to lower base rates.

Average card balances increased by 29 per cent, and interest income related to credit cards rose significantly in the Middle East, India and Australia. In the Middle East, credit card balances rose following the success of efforts to increase cardholder spending and the number of cards in circulation. The latter rose by 12 per cent in the first half of 2008 to over 1.3 million. Total cards in issue in the Rest of Asia-Pacific region exceeded 9.3 million. Spreads on credit card lending widened, driven by the Middle East and India, where base rate cuts led to lower funding costs while asset pricing was maintained.

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In Indonesia and India, lending growth, including personal instalment loans and cards, continued following the expansion of the consumer finance business begun in 2007 which continued in Indonesia with the addition of 24 branches. Spreads in each of these countries improved due to higher lending rates combined with stable base rates.

Net fee income increased by 23 per cent to US$434 million, with growth in cards and the sale of investment products. Credit card fee income increased by 33 per cent, driven by higher balances, cardholder spending and new cards in the Middle East and India. Funds under management continued to grow, reaching US$13.1 billion. Sales of investment products increased despite stock market volatility, as customers increasingly chose structured products over market-led unit trusts. HSBC increased fees from the sale of insurance products by 41 per cent as a result of new product launches, including credit enhancement insurance.

Declines in global equity markets resulted in lower net claims, however this was offset by a corresponding net loss on investments held by the insurance business.

Loan impairment charges rose by 43 per cent, driven by higher charges in India, the Middle East and, to a lesser extent, Australia. The main contributing factors in India were volume growth, seasoning of the personal lending portfolio, higher delinquency on credit cards and personal loans and a challenging collections environment. In the Middle East, volume growth of the credit card portfolio led to a rise in delinquency, notably in the UAE. Loan impairment charges increased by 83 per cent in Australia due to increased delinquencies on cards.

In Taiwan, loan impairment charges decreased by 67 per cent, due to an improvement in asset quality and increased collection efforts in the high risk segments.

HSBC continued to invest substantially in the region, particularly in India and mainland China. The number of staff increased in key markets including mainland China and the Middle East. Further branches in mainland China led to the hiring of over 800 additional staff. Deteriorating credit performance and increased loan delinquencies in the consumer finance business drove a rise in fees paid to collection agencies in India and Indonesia. In Japan, *operating expenses* increased, primarily due to the launch of Premier and branch expansion. Cost increases were controlled in part by customer use of low-cost channels. In the UAE, the number of e-Saver accounts increased by 204 per cent, along with a 96 per cent rise in internet transactions.

Income from associates rose substantially and was 79 per cent higher than in the first half of 2007. HSBC s associate, Ping An Insurance, continued to be successful in increasing life insurance premiums, which, combined with an increase to long-term yield assumptions led to increased embedded value. In addition, contributions from Bank of Communications and The Saudi British Bank rose by 95 per cent and 146 per cent, respectively. The increase in the latter was primarily attributable to strong asset growth and limited loan impairment charges. The Saudi British Bank also launched three Premier centres.

Commercial Banking reported a pre-tax profit of US$961 million, 52 per cent higher than in the first half of 2007. Growth was largely attributable to mid-market and small business customer acquisition, and increased associates income from the Bank of Communications and Industrial Bank in mainland China. Revenue growth across the region was largely volume driven and the credit environment remained relatively benign. Asian intra-regional trade and investment flows continued to strengthen, mitigating the effects of the global economic slowdown. Notwithstanding the expansion of the network to second tier cities in India, Taiwan and mainland China and an increase in staff numbers, the cost efficiency ratio remained broadly in line with the first half of 2007.

In the Middle East, profit before tax rose by 41 per cent, as buoyant economic conditions across the region contributed to notable customer and revenue growth. Additional staff were recruited to increase sales of trade services and actively manage relationships with customers of trade and supply-chain products.

In mainland China, operating profit grew by 46 per cent as HSBC continued to strengthen the local distribution network, adding a further branch in the first half of 2008 to supplement volume growth in deposits. The Greater China regional model continued to show strong results, demonstrated by a 163 per cent growth in the number of referrals from mainland China through Global Links, the cross-border referral system. Though hindered by restrictions on local currency lending imposed by the People s Bank of China, HSBC continued to grow revenues by repricing assets and fee-based business.

Profit before tax in Singapore declined by 32 per cent, largely due to reduced net interest income as lower interest rates resulted in compressed margins on current accounts. This was partially offset by an increased focus on income generation

from fund and ancillary services, augmented by net recoveries of loan impairment charges.

In India, profit before tax rose by 47 per cent to US$75 million. Strong revenue growth in the country was driven by increased customer acquisition, particularly in second tier cities. This growth was supplemented by stronger bilateral business flows with Mauritius and higher deposit balances.

In Malaysia, profit before tax increased by 68 per cent, as loan impairment charges improved in comparison with the first half of 2007. Revenues increased by 12 per cent, due to growth in deposit and asset balances which more than offset the effect of narrower spreads for foreign currency deposits.

Profit before tax in Australia increased by 86 per cent. Revenue growth was broad-based with interest income growth of 36 per cent attributable to increased deposit balances.

HSBC further enhanced its cross-border business capabilities with the opening of a new International Banking Centre in Japan, taking coverage to 27 countries and territories in the region. Successful referral volumes originating within the Asia-Pacific region from Global Links, the cross-border referral system, more than doubled compared with the first half of 2007.

Net interest income increased by 25 per cent, due largely to growth in deposit volumes from enhanced focus on generating both local and foreign currency balances. Lower interest rates contributed to the contraction of liability and asset spreads, and to lower earnings from free funds.

Lending volumes rose by 22 per cent, particularly in India and the Middle East. In India, growth was spurred by an increase in customer numbers across all segments and product groups, along with higher spreads on customer advances. Receivables finance also reported increased income in India. Favourable economic conditions in the Middle East contributed to increased lending volumes, and spreads increased on corporate lending products, as pricing resulted in higher yields. Branch expansion in mainland China succeeded in increasing customer numbers by 29 per cent and driving lending growth.

Average deposit balances increased by 16 per cent, notwithstanding lower margins. In India, deposit volumes benefited from increased customer numbers. Customer numbers also rose in the Middle East and, with HSBC s focus on payments and cash management, contributed to a 37 per cent rise in deposit balances. Lower interest rates caused spreads

on deposits to reduce in India, the Middle East and mainland China.

Net fee income rose by 37 per cent to US$290 million, predominantly driven by growth in fees from trade services products, notably in the Middle East and mainland China.

Trade-related lending fees rose by 36 per cent, largely in the Middle East as international and trading activity in the region remained strong, but also in India, Malaysia, South Korea and Australia. In the Middle East, volume growth was enhanced by inflation-induced increases in commodity prices, notably on materials vital to the booming construction industry. HSBC s distribution capabilities in the region also contributed to growth. HSBC s positioning in Dubai, a key trading market and international hub, resulted in over 65 per cent growth in import and export trading volumes in the UAE, along with similar growth in fees from trade and supply chain activities. In mainland China, growth in forfaiting led to a 32 per cent increase in trade-related fees. Customer acquisition in India drove significant volume increases in fees from trade services and payments and cash management.

Trading income grew by 70 per cent, mainly due to growth in volumes of transactions in the Middle East and in India, attributable to increased volatility in the foreign exchange markets. Within the Middle East, higher trading income also reflected growth in the total value of transactions due to the effects of inflation and increased remittances.

Loan impairment recoveries of US$16 million were largely due to the non-recurrence of downgrades to certain customers in Thailand and Malaysia. In addition benign credit conditions continued in the Middle East with net releases more than doubling.

Total *operating expenses* rose by 33 per cent, driven by rising staff costs across the majority of the region. Investment was undertaken to expand HSBC s presence, notably in mainland China. Customer facing staff numbers increased across the region by 30 per cent to support business expansion. In the Middle East, increased staff numbers, wage inflation driven by competitive labour market conditions and higher performance related pay as a consequence of improved profits caused a 30 per cent rise in staff costs. Cost growth in India was principally due to geographical expansion into second tier cities and growth in the number of relationship managers.

The percentage of total transactions completed using lower-cost channels increased compared with

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the first half of 2007. Over 3.5 million transactions were completed using these channels and the number of customers registered for business internet banking rose by 43 per cent.

HSBC s associate, Bank of Communications, increased its contribution by 67 per cent, driving a 63 per cent increase in *income from associates*. Bank of Communications continued to expand its operations in mainland China. The contribution from Industrial Bank also increased compared with the first half of 2007 due to growth and rising margins.

Global Banking and Markets profit before tax rose by 71 per cent to US$2.0 billion, with growth in all major countries, with notable improvements in the Middle East, South Korea, mainland China and India.

In the Middle East, pre-tax profit doubled due to a combination of strong growth in foreign exchange trading and a robust contribution from Global Banking and Balance Sheet Management. Securities services profit also grew, reflecting the importance of the region for the securities services strategy. Global Banking increased lending, taking advantage of strong economic growth in the region and wider spreads. Balance Sheet Management profit was higher due to a lower cost of funds as local central banks reduced interest rates in line with the US.

In India, higher pre-tax profit was attributable to foreign exchange trading and securities services. Foreign exchange profits were driven by high customer demand and market volatility. The increased securities services profit was due to growth in deposit account balances and in the derivatives clearing business.

Pre-tax profit in mainland China rose substantially, driven by Balance Sheet Management, which earned higher revenues due to an increase in surplus funds as the People s Bank of China restricted lending, combined with a steepening yield curve. Rates and foreign exchange trading also performed strongly, as did income from associates as Ping An Insurance and Bank of Communications expanded. Ping An Insurance continued to grow its asset management business, while Bank of Communications earned increased fees for asset custody and advisory work.

Balance Sheet Management was the main reason for increased profits in Singapore, benefiting from the reduction in short-term US and Singapore dollar interest rates.

In South Korea, pre-tax profits grew as Rates performed strongly, driven by increased client

demand for hedging products linked to financing activity.

In Malaysia, Rates and foreign exchange were the main contributors to profit growth. Significant client activity was driven by market volatility as inflationary expectations triggered a sharp upward move in interest rates, leading clients to demand products which protected them from interest and exchange rate risks.

The region s total operating income grew by 55 per cent to US$2.4 billion. Foreign exchange trading delivered strong revenues throughout the region. During the first half of 2008 there was significant volatility in the foreign exchange markets contributing to increased trading and strong customer demand for foreign exchange products, while HSBC s broad distribution network helped to attract clients. Balance Sheet Management benefited in most countries from the steepening of the yield curve as central banks responded to the credit market turmoil.

Net interest income increased by 58 per cent due to the strong performance of Balance Sheet Management, described above, and also growth in the Middle East as average customer lending rose by more than 40 per cent due to overall investment in infrastructure and business expansion in the region, and widening spreads.

Net fee income grew by 29 per cent, driven by the ongoing strength of the securities services and payments and cash management businesses. Transaction volumes and growing client balances drove the increase in payments and cash management. In securities services, higher client trading volumes increased the level of transactions which led to higher fees in the custody and clearing business. Global Asset Management also reported an increase in fees, as funds under management benefited from inflows of new funds and new product launches, despite declining local stock markets.

Trading income rose significantly, driven by foreign exchange products, as noted above. Foreign exchange trading income increased by 68 per cent, continuing its strong upward momentum. Rates trading in South Korea also contributed, in response to increased client activity in local rates markets and hedging relating to financing activity.

Gains less losses from financial investments were lower due to the non-recurrence of significant disposals in 2007 in the Philippines.

The corporate credit environment remained benign, with a very low *loan impairment charge*.

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Nonetheless, this compared unfavourably with the first half of 2007 due to releases in Singapore and South Korea.

Operating expenses rose as the business invested to support growth across the region, driving an increase in staff numbers, with rises in most countries. Salary levels also rose, in line with inflation. Higher profits across the region also led to increased performance-related costs.

Private Banking reported a pre-tax profit of US$54 million, a decrease of 4 per cent when compared with the first half of 2007. Strong revenue growth continued in Singapore with a large rise in deposits. Higher profits were also recorded in India, notwithstanding further investment. Overall, the cost efficiency ratio worsened by 8.4 percentage points to 57.5 per cent, as a result of investment in domestic operations in a number of countries.

A 33 per cent rise in customer deposits in Singapore to US$9.4 billion was the main reason for a 68 per cent increase in *net interest income*. This trend was due to customers switching from investment securities to cash deposits in response to the turbulence in the equity markets.

Other revenues decreased by 2 per cent to US$80 million, as the demand for equity-linked structured products declined as the Hong Kong equity market underperformed in the first half of

the year. However, this was partly offset by a US$6 million growth in *trading income* in Japan from clients active in foreign exchange trading.

Client assets increased by 3 per cent to US$20.9 billion, with net new money of US$1.6 billion partly offset by a lower market valuation compared with 31 December 2007. The growth in cross-referrals continued, with inward referrals from other customer groups contributing US$168 million to total client assets, compared with US$66 million in the first half of 2007.

Operating expenses rose by 35 per cent to US$73 million, driven by market related pressures in Singapore. Business expansion, particularly in Japan and the new Private Banking offices in mainland China, also contributed to the rise in staff, property and IT costs.

Profit before tax reported within the **Other** segment was US$102 million. The costs and related recharges of HSBC s 15 GSCs, located primarily in mainland China and India, are reported in Other. Costs at GSCs increased by 9 per cent to US$286 million, due to increased volumes of activities undertaken and the opening of 4 new centres in the second half of 2007. This growth was supported by a 14 per cent rise in staff numbers. Costs are recovered from Group entities and recorded as other operating income.

Reconciliation of reported and underlying profit before tax

	Half-year to 30 June 2008 (1H08) compared with half-year to 31 December 2007 (2H07)								
Rest of Asia-Pacific (including the Middle East)	2H07 as reported US$m	Disposals and dilution gains[1] US$m	Currency translation[2] US$m	2H07 at 1H08 exchange rates US$m	Acqui-sitions[1] US$m	Under-lying change US$m	1H08 as reported US$m	Re-ported change %	Under-lying change %
Net interest income	2,242		53	2,295	8	330	2,633	17	14
Net fee income	1,236		32	1,268	1	69	1,338	8	5
Other income[3]	1,343	(5)	14	1,352	4	514	1,870	39	38

Net operating income[4]	4,821	(5)	99	4,915	13	913	5,841	21	19
Loan impairment charges and other credit risk provisions	(308)		(1)	(309)		(60)	(369)	(20)	(19)
Net operating income	4,513	(5)	98	4,606	13	853	5,472	21	19
Operating expenses	(2,689)		(57)	(2,746)	(11)	(27)	(2,784)	(4)	(1)
Operating profit	1,824	(5)	41	1,860	2	826	2,688	47	44
Income from associates	841		37	878		58	936	11	7
Profit before tax	2,665	(5)	78	2,738	2	884	3,624	36	32

For footnotes, see page 89.

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Analysis by customer group and global business

Profit before tax

	Half-year to 30 June 2008						
Rest of Asia-Pacific (including the Middle East)	**Personal Financial Services US$m**	**Commercial Banking US$m**	**Global Banking and Markets US$m**	**Private Banking US$m**	**Other US$m**	**Inter-segment elimination[9] US$m**	**Total US$m**
Net interest income	1,166	680	918	47	88	(266)	2,633
Net fee income	434	290	560	43	11		1,338
Trading income/(expense) excluding net interest income	53	104	829	36	(30)		992
Net interest income/(expense) on trading activities	(2)		82		(9)	266	337
Net trading income/(expense)[7]	51	104	911	36	(39)	266	1,329
Net expense from financial instruments designated at fair value	(85)	(1)	(2)				(88
Gains less losses from financial investments	28	3	1		1		33
Gains arising from dilution of interests in associates							
Dividend income			2				2
Net earned insurance premiums	98	16					114
Other operating income	30	12	42	1	522	(123)	484
Total operating income	1,722	1,104	2,432	127	583	(123)	5,845
Net insurance claims[8]	6	(9)			(1)		(4
Net operating income[4]	1,728	1,095	2,432	127	582	(123)	5,841
Loan impairment (charges)/recoveries and other credit risk provisions	(375)	16	(11)		1		(369
Net operating income	1,353	1,111	2,421	127	583	(123)	5,472
Total operating expenses	(1,187)	(441)	(701)	(73)	(505)	123	(2,784
Operating profit	166	670	1,720	54	78		2,688
Share of profit in associates and joint ventures	369	291	252		24		936
Profit before tax	535	961	1,972	54	102		3,624
	%	%	%	%	%		%
Share of HSBC s profit before tax	5.2	9.4	19.2	0.5	1.1		35.4
Cost efficiency ratio	68.7	40.3	28.8	57.5	86.8		47.7

Balance sheet data[6]

	US$m	US$m	US$m	US$m	US$m		US$m
Loans and advances to customers (net)	37,861	37,384	35,001	3,350	161		113,757

Total assets	**43,684**	**42,833**	**153,733**	**8,413**	**10,378**		**259,041**
Customer accounts	**56,552**	**38,968**	**58,162**	**12,594**	**519**		**166,795**
Loans and advances to banks (net)[12]			**39,583**				
Trading assets[12,13]			**40,477**				
Financial instruments designated at fair value[12]			**27**				
Financial investments[12]			**40,631**				
Deposits by banks[12]			**20,113**				
Trading liabilities[12,13]			**25,659**				

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Interim Management Report: Business Review (continued)

Analysis by customer group and global business *(continued)*

Profit before tax

Rest of Asia-Pacific (including the Middle East)	Half-year to 30 June 2007						
	Personal Financial Services US$m	Commercial Banking US$m	Global Banking and Markets US$m	Private Banking US$m	Other US$m	Inter-segment elimination[9] US$m	Total 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[7]	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/(expense)	20	8	20	(6)	387	(69)	360
Total operating income	1,460	801	1,494	109	1,566	(69)	5,361
Net insurance claims[8]	(137)	(4)					(141)
Net operating income[4]	1,323	797	1,494	109	1,566	(69)	5,220
Loan impairment charges and other credit risk provisions	(252)	(54)	(2)				(308)
Net operating income	1,071	743	1,492	109	1,566	(69)	4,912
Total operating expenses	(911)	(313)	(510)	(53)	(357)	69	(2,075)
Operating profit	160	430	982	56	1,209		2,837
Share of profit in associates and joint ventures	191	167	116		33		507
Profit before tax	351	597	1,098	56	1,242		3,344

	%	%	%	%	%		%
Share of HSBC s profit before tax	2.5	4.2	7.8	0.4	8.8		23.6
Cost efficiency ratio	68.9	39.3	34.1	48.6	22.8		39.8

Balance sheet data[6]

	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)[12]			28,663				
Trading assets[12,13]			27,699				
Financial instruments designated at fair value[12]			979				
Financial investments[12]			27,269				
Deposits by banks[12]			12,860				
Trading liabilities[12,13]			16,810				

For footnotes, see page 89.

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Profit before tax

Rest of Asia-Pacific (including the Middle East)	Personal Financial Services US$m	Commercial Banking US$m	Global Banking and Markets US$m	Private Banking US$m	Other US$m	Inter-segment elimination[9] US$m	Total US$m
	Half-year to 31 December 2007						
Net interest income	1,051	614	744	32	87	(286)	2,242
Net fee income	430	227	543	33	3		1,236
Trading income/(expense) excluding net interest income	38	71	525	36	(74)		596
Net interest income/(expense)on trading activities	(1)		(36)		1	286	250
Net trading income/(expense)[7]	37	71	489	36	(73)	286	846
Net income/(expense) from financial instruments designated at fair value	18	1	(8)	(1)	23		33
Gains less losses from financial investments	3		9				12
Gains arising from dilution of interests in associates					5		5
Dividend income			1		3		4
Net earned insurance premiums	109	7			1		117
Other operating income	20	7	33	8	462	(92)	438
Total operating income	1,668	927	1,811	108	511	(92)	4,933
Net insurance claims[8]	(109)	(3)					(112)
Net operating income[4]	1,559	924	1,811	108	511	(92)	4,821
Loan impairment charges and other credit risk provisions	(300)	(7)	(1)				(308)
Net operating income	1,259	917	1,810	108	511	(92)	4,513
Total operating expenses	(1,220)	(426)	(630)	(72)	(433)	92	(2,689)
Operating profit	39	491	1,180	36	78		1,824
Share of profit in associatesand joint ventures	370	262	186		23		841
Profit before tax	409	753	1,366	36	101		2,665
	%	%	%	%	%		%
Share of HSBC s profit before tax	4.1	7.5	13.6	0.4	1.0		26.5
Cost efficiency ratio	78.3	46.1	34.8	66.7	84.7		55.8

Balance sheet data[6]

	US$m	US$m	US$m	US$m	US$m	US$m
Loans and advances to customers (net)	34,486	32,159	32,106	2,955	146	101,852
Total assets	40,092	37,215	133,814	7,561	9,430	228,112
Customer accounts	49,703	34,891	54,120	11,116	403	150,233
Loans and advances to banks (net)[12]			30,853			
Trading assets[12,13]			29,966			
Financial instruments designated at fair value[12]			43			
Financial investments[12]			39,448			
Deposits by banks[12]			17,174			
Trading liabilities[12,13]			18,257			

For footnotes, see page 89.

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Interim Management Report: Business Review (continued)

North America

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

	Personal Financial Services US$m	Commercial Banking US$m	Global Banking and Markets US$m	Private Banking US$m	Other US$m	Total US$m
Half-year to 30 June 2008						
US	**(2,194)**	**167**	**(1,779)**	**48**	**277**	**(3,481)**
Canada	**127**	**237**	**119**	**4**	**7**	**494**
Bermuda	**17**	**26**	**35**	**6**	**10**	**94**
	(2,050)	**430**	**(1,625)**	**58**	**294**	**(2,893)**
Half-year to 30 June 2007						
US	1,336	215	292	50	(44)	1,849
Canada	145	222	120	4	2	493
Bermuda	7	40	24	6	16	93
	1,488	477	436	60	(26)	2,435
Half-year to 31 December 2007						
US	(3,160)	162	(1,535)	106	1,512	(2,915)
Canada	120	244	119	4	3	490
Bermuda	6	37	15	4	18	80
Other					1	1
	(3,034)	443	(1,401)	114	1,534	(2,344)

Loans and advances to customers (net) by country

	At 30 June 2008 US$m	At 30 June 2007 US$m	At 31 December 2007 US$m
US	**215,909**	233,592	233,706
Canada	**54,346**	45,510	53,891
Bermuda	**2,235**	2,193	2,263
	272,490	281,295	289,860

Customer accounts by country

	At 30 June 2008 US$m	At 30 June 2007 US$m	At 31 December 2007 US$m
US	**95,763**	93,325	100,034
Canada	**38,367**	32,744	37,061
Bermuda	**7,870**	8,328	8,078
	142,000	134,397	145,173

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Profit/(loss) before tax

	Half-year to		
North America	**30 June 2008 US$m**	30 June 2007 US$m	31 December 2007 US$m
Net interest income	**7,873**	7,307	7,540
Net fee income	**2,822**	2,904	2,906
Net trading income/(expense)	**(1,816)**	622	(1,164)
Net income from financial instruments designated at fair value	**368**	81	1,669
Gains less losses from financial investments	**106**	53	192
Dividend income	**40**	64	41
Net earned insurance premiums	**203**	231	218
Other operating income	**115**	342	18
Total operating income	**9,711**	11,604	11,420
Net insurance claims incurred and movement in liabilities to policyholders	**(112)**	(124)	(117)
Net operating income before loan impairment charges and other credit risk provisions	**9,599**	11,480	11,303
Loan impairment charges and other credit risk provisions	**(7,166)**	(3,820)	(8,336)
Net operating income	**2,433**	7,660	2,967
Total operating expenses	**(5,334)**	(5,235)	(5,321)
Operating profit/(loss)	**(2,901)**	2,425	(2,354)
Share of profit in associates and joint ventures	**8**	10	10
Profit/(loss) before tax	**(2,893)**	2,435	(2,344)
	%	%	%
Share of HSBC s profit before tax	**(28.2)**	17.2	(23.3)
Cost efficiency ratio	**55.6**	45.6	47.1
Period-end staff numbers (full-time equivalent)	**48,069**	56,693	52,722

Balance sheet data[6]

	US$m	US$m	US$m
Loans and advances to customers (net)	**272,490**	281,295	289,860
Loans and advances to banks (net)	**19,794**	18,643	16,566
Trading assets, financial instruments designated at fair value, and financial investments16	**133,262**	149,004	133,998
Total assets	**531,607**	519,693	510,092
Deposits by banks	**11,764**	13,043	16,618
Customer accounts	**142,000**	134,397	145,173

For footnotes, see page 89.

Economic briefing

In the **US**, GDP growth was subdued during the early months of 2008, but appeared to develop some momentum in the second quarter in response to fiscal loosening. Housing activity again proved weak, with certain measures of house prices showing large declines in a number of regions, although tentative signs emerged of stability in housing sales, albeit at subdued levels. The rise in mortgage delinquencies remained of primary concern. Employment conditions weakened throughout the first half of 2008, with the unemployment rate rising from 5.0 per cent in December 2007 to 5.5 per cent in June 2008. Concerns over the labour market

appeared to influence consumer confidence although, for the most part, consumer spending proved resilient. Consumer price inflation remained high throughout the first half of 2008, standing at 5.0 per cent in June 2008. This was largely due to rising energy prices; excluding food and energy, consumer price inflation averaged 2.4 per cent during the period. The Federal Reserve lowered short-term interest rates by 225 basis points to 2 per cent in the first half of 2008, in an attempt to mitigate the worst effects of the sub-prime related credit squeeze on financial markets and economic activity. Declines in the second quarter of 2008 left Standard & Poor s S&P500 stock market index about 13 per cent below its level at the end of 2007.

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Canadian GDP increased by just 1.2 per cent during the first five months of 2008 compared with the equivalent period in 2007, despite robust growth in consumer and government expenditure. Labour market conditions suffered a slight deterioration, although the unemployment rate of 6.2 per cent in June 2008 was only marginally above the historical low of 5.8 per cent recorded in October 2007. The

headline rate of consumer price inflation fluctuated at around 2 per cent during the first half of 2008 before moving to a level of 3.1 per cent, year-on-year, in June, while the level of core inflation held below the 1.5 per cent mark. The Bank of Canada cut its overnight interest rate from 4.25 per cent at the end of 2007 to 3 per cent in April 2008.

Reconciliation of reported and underlying profit before tax

Half-year to 30 June 2008 (1H08) compared with half-year to 30 June 2007 (1H07)

North America	1H07 as reported US$m	Disposals and dilution gains[1] US$m	Currency translation[2] US$m	1H07 at 1H08 exchange rates US$m	Acqui-sitions[1] US$m	Under-lying change US$m	1H08 as reported US$m	Re-ported change %	Under-lying change %
Net interest income	7,307		70	7,377		496	7,873	8	7
Net fee income	2,904	(52)	26	2,878		(56)	2,822	(3)	(2)
Other income/(expense)[3]	1,269		7	1,276		(2,372)	(1,096)	(186)	(186)
Net operating income[4]	11,480	(52)	103	11,531		(1,932)	9,599	(16)	(17)
Loan impairment charges and other credit risk provisions	(3,820)		(3)	(3,823)		(3,343)	(7,166)	(88)	(87)
Net operating income	7,660	(52)	100	7,708		(5,275)	2,433	(68)	(68)
Operating expenses	(5,235)	50	(52)	(5,237)		(97)	(5,334)	(2)	(2)
Operating profit/(loss)	2,425	(2)	48	2,471		(5,372)	(2,901)	(220)	(217)
Income from associates	10			10		(2)	8	(20)	(20)
Profit/(loss) before tax	2,435	(2)	48	2,481		(5,374)	(2,893)	(219)	(217)

For footnotes, see page 89.

Review of business performance

HSBC s North America operations reported a pre-tax loss of US$2.9 billion in the first half of 2008, compared with a pre-tax profit of US$2.4 billion in the first half of 2007, a decline of 219 per cent, and 217 per cent on an underlying basis. The pre-tax loss was US$549 million more than in the second half of 2007.

The US economy was weak in the first half of 2008, with unemployment rising despite resilience in some sectors. It is now generally believed that the deterioration in the housing market will be deeper and longer in terms of its effect on housing prices, and that it will extend into 2009. Credit quality continued to deteriorate in much of the US loan book, including some increase in impairment in prime mortgage lending at the US retail bank, which is HSBC Bank USA, excluding its consumer finance operations. The US economy continued to weaken and credit conditions deteriorated in the first half of 2008. As a result, US$527 million of goodwill carried by North America Personal Financial Services was impaired. For further information see Note 20 to the Financial Statements. Loan

impairment charges rose by 88 per cent and the Personal Financial Services business recorded a pre-tax loss of US$2.1 billion. Profit before tax in Canada was broadly in line with the first half of 2007 at US$494 million, as the economy remained relatively strong.

The turmoil in the global credit markets persisted into 2008 and became more pronounced, leading to a loss before tax of US$1.6 billion in Global Banking and Markets. Further write-downs in credit trading positions, structured credit derivatives, leveraged and acquisition finance loans, and exposures to monoline insurers were only partly offset by strong performances in foreign exchange, equities, rates, metals trading, and payments and cash management. Commercial Banking profits declined by 10 per cent, as revenues fell due to tighter deposit spreads despite strong growth in balances, while loan impairment charges increased from the low levels of 2007. Pre-tax profits in Private Banking declined, as lower fee income more than offset the reduction in operating expenses driven by lower staff costs. Profit before tax in Bermuda was in line with the first half of 2007.

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The following commentary is on an underlying basis.

Personal Financial Services reported a pre-tax loss of US$2.1 billion, a decline of US$3.5 billion from the first half of 2007.

Deteriorating economic conditions led to a significant rise in loan impairment charges as credit quality worsened. This more than offset the reduction in operating costs delivered by management actions in the consumer finance business such as closing branches, reduced marketing, discontinuing certain Taxpayer Financial Services products and relationships, restricting vehicle finance business and further tightening underwriting criteria across the loan portfolio. Impairment of goodwill was the primary driver of the 3 per cent rise in operating expenses. HSBC acted to mitigate the effect of the housing market decline on customers, with more loans modified and loan modification periods extended.

In the US, pre-tax losses in the first half of 2008 of US$2.2 billion compared with a US$1.3 billion profit in the same period in 2007. Losses were driven by increased loan impairment charges, as credit quality declined due to a combination of falling house prices, rising unemployment, higher fuel and food costs and tighter credit conditions. Portfolio seasoning also contributed to higher loan impairment charges. The turmoil in credit markets continued and debt securitisation activity remained very low. This severely reduced the number of refinancing options available to customers. Historically, customers facing financial hardship from unforeseen life events such as redundancy or ill-health have used mortgage refinancing to withdraw equity from their homes to meet their financial obligations. Reduced refinancing opportunities have increased the risk that these customers may default on some or all of their loan obligations. In response, management in the consumer finance business launched intensive programmes to limit foreclosures, modifying more than 34,000 loans. Losses incurred on repossessed properties were partly offset by one-off gains of US$129 million from the Visa IPO. Interest expense fell due to lower funding costs, while staff and marketing costs were lower following management action to reposition the business.

In Canada, profit before tax declined by 18 per cent to US$127 million as higher net interest income due to growth in lending and deposits following effective marketing campaigns was more than offset by an increase in loan impairment charges in the consumer finance business. This was driven by

deteriorating delinquency trends in mortgages and private label cards, as the consumer credit environment became more challenging in Western Canada. An expansion of the branch network of the Canadian retail bank, HSBC Bank Canada, and an increase in employee numbers resulted in increased administrative and staff costs.

Net interest income was in line with the first half of 2007, notwithstanding a 3 per cent fall in average loan balances. Spreads widened due to a significant reduction in funding costs following central bank rate cuts, together with the mix effect from an increased proportion of higher yielding credit and private label cards. These factors were partly offset by a decline in US lending balances, increased impaired loans and lower prepayment volumes.

In the US, net interest income was unchanged. US average deposit balances rose by 5 per cent, as online savings account and retail network savings and current account balances increased. At 30 June 2008, online savings account balances were US$13 billion, with customer numbers rising to over 860,000, attracted by the effect of promotional rates. The number of Premier customers rose by 17 per cent in the twelve months since 30 June 2007 to 215,000, due to marketing campaigns and sales efficiency improvements. Deposit spreads narrowed, reflecting a significant decline in base rates and the change in product mix to higher yielding savings accounts.

Average US mortgage balances declined by 11 per cent to US$112 billion, primarily due to the winding down of the mortgage services portfolio, the tightening of credit criteria for new lending and portfolio sales at the US retail bank and consumer finance business. The slowdown in the US housing market intensified in the first half of 2008, with prices, sales and new housing construction all declining and thereby reducing loan demand.

In the consumer finance business, spreads across the total mortgage loan portfolio widened as funding costs declined due to a 325 basis point reduction in US short-term interest rates compared with 30 June 2007.

Average mortgage balances in the branch-based consumer lending business increased by 5 per cent to US$50 billion due to growth in the second half of 2007. During the first six months of 2008, liquidations exceeded new originations, the latter declining sharply as a result of the closure of some 400 branches during 2007, with another 100 closed in 2008, and further tightening of underwriting standards. This was partly offset by lower run-off rates as a result of the decline in loan prepayments.

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Yields declined due to deteriorating credit quality as the volume of impaired loans increased and loan terms were modified downwards. A slowdown in the rate of liquidations mitigated the effect of lower originations but also led to lower prepayment penalty income and reduced revenues from amortisation of deferred loan origination fees. Yields on new lending rose despite tighter underwriting criteria which led to a change in mix towards higher quality assets that typically price at a lower level. Spreads widened as funding costs declined.

In mortgage services, average mortgage balances declined by 28 per cent to US$34 billion, largely due to liquidations in the normal course of business following the cessation of new originations in 2007. The pace of decline was partly moderated by lower loan prepayments due to fewer refinancing opportunities for customers. Spreads narrowed as lower funding costs were more than offset by a fall in yields as deteriorating credit quality led to lower levels of early repayment due to reduced prepayment penalty income.

Average mortgage balances held by the US retail bank declined by 10 per cent to US$28 billion as the bank continued to sell a majority of its new residential mortgage loan originations to government-sponsored enterprises and private investors, and allow its residential mortgage loan portfolio to run off including a US$4 billion portfolio sale in the first half of 2008. Spreads widened as yields declined by less than funding costs in the falling rate environment.

Average credit and private label card balances at 30 June 2008 were US$49 billion. Lending growth slowed to 4 per cent as HSBC reduced marketing and tightened underwriting standards during the second half of 2007 and into 2008. Spreads widened as yields declined less than funding costs. Yields declined, driven by changes in product mix in credit and private label cards. Partly offsetting this was the effect of card balances at their contractual floor.

Vehicle finance average balances were broadly flat. Growth in the near-prime portfolio was the result of expansion in the customer direct loan programme, partly offset by lower originations in the dealer network portfolio due to action taken in the second half of 2007 to improve the credit quality of new lending. In the first quarter of 2008, HSBC discontinued dealer relationships in several states, primarily in the Northeast, and withdrew some products. Spreads widened as yields increased and cost of funds declined. Yields increased due to an increased proportion of higher yielding consumer

finance loans, partly offset by changes in product mix towards lower yielding, lower risk loans.

In late July 2008 HSBC decided to cease originating new business within a 90-day period in the North America vehicle finance business of HSBC Finance Corporation. While credit quality in the vehicle finance business had improved during the first half of 2008, management considered that the business was sub-scale and did not have sufficient market strength for it to provide an acceptable level of risk adjusted returns. HSBC will manage an orderly run-off of the portfolio of US$12.5 billion. The estimated costs associated with the decision to exit the vehicle finance business are US$25 million, a substantial portion of which are expected to be recognised in the second half of 2008.

Personal non-credit card average balances declined by US$865 million as a result of actions taken to tighten underwriting standards in 2007. Despite a fall in funding costs, spreads narrowed as yields declined.

In Canada, net interest income rose by 11 per cent, primarily due to a 10 per cent increase in average lending balances, reflecting house price appreciation since the first half of 2007 and robust economic growth. Deposit balances rose, primarily reflecting growth in customer numbers. Premier customer numbers increased by more than 25,000 to over 93,000. Yields fell across most lending products as falling base rates were passed on to floating rate customers, while yields on deposits rose as competition increased. Spreads tightened across the majority of the portfolio as wider credit spreads meant base rate cuts were not fully reflected in funding costs.

Average deposit balances in Canada rose by 9 per cent, driven by strong growth in the direct savings account as HSBC increased its share of the market. Average balances in the high rate and direct savings accounts more than doubled to US$2.9 billion driven by a combination of new customer acquisition and higher average balances on existing accounts. Deposit spreads tightened as yields on deposits rose, despite lower base rates due to an increase in the mix of higher yielding savings accounts and as competition between deposit taking institutions intensified. Yields on surplus funds were broadly unchanged.

Average lending balances in Canada were 10 per cent higher, driven by demand for credit in a relatively robust economy. Lending in consumer finance rose, due to growth in the private label card portfolio, following a significant new relationship in the second half of 2007. In the Canadian retail bank,

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lending rose driven by mortgages and other personal lending as economic growth continued. Yields declined across most products as interest rate cuts were immediately passed on to floating rate borrowers while overall spreads tightened despite lower base rates as credit spreads widened.

Fee income declined by 8 per cent, mainly due to changes to fee billing practices in the credit card business and the withdrawal of some products in Taxpayer Financial Services. In the US, fees fell by 9 per cent. Fee income from credit cards declined due to changes in overlimit fee billings implemented during the fourth quarter of 2007 and first half of 2008 to improve the customer proposition. A decline in credit quality, changes to the portfolio mix and higher balances led to an increase in the level of uncollectible fees in the credit card and private label portfolios. Fees for late payment rose due to an increase in overdue balances, changes in the merchant mix and amendments to terms. Enhancement services revenue rose as higher take-up rates led to increased fees from debt protection products and total insurance fee income increased by 34 per cent to US$390 million. Taxpayer Financial Services revenue decreased as a result of discontinuing pre-season and pre-file loan products for the 2008 tax season and the decision to reduce the number of relationships with third parties.

At the US retail bank, net fee income rose by 29 per cent to US$372 million, driven by higher service charges on deposits and increased credit card fees from higher transaction volume.

Fee income in Canada rose by 4 per cent. In the Canadian retail bank, the rise was driven by higher service charges, due to repricing; investment administration fees, as a result of growth in funds under management; foreign exchange fees, arising from increased client volumes resulting from volatility in the Canadian dollar to US dollar exchange rate; and Global Immigrant Investor Programme fees, due to growth in volumes. Fee income in consumer finance fell by 7 per cent from a low base in the first half of 2007.

Trading losses declined to US$16 million from US$97 million in the first half of 2007, due to the closure of the Decision One brokerage business.

The Visa IPO provided a US$92 million *gain on financial investments*.

Other operating income declined by 189 per cent, primarily due to losses on repossessed properties as volumes increased and values fell with the decline in house prices. In the consumer finance business, total foreclosed properties rose to nearly

11,000 from over 9,600 at 31 December 2007 although, following operational enhancements, the time which foreclosed assets remained on the market fell from 183 days to 171 days.

Other operating income in Canada fell, largely reflecting a net loss on the sale of a mortgage brokerage business within consumer finance. Other operating income fell in the Canadian retail bank due to the non-recurrence of a gain on the sale of shares in the Montreal stock exchange in the first half of 2007.

Loan impairment charges rose by 84 per cent on the first half of 2007 to US$7.0 billion, driven by a weakening US economy, continued deterioration in the consumer finance loan portfolio and a decline in the credit quality of prime and second lien mortgages held by HSBC Bank USA. Charges were US$1.2 billion lower than in the second half of 2007. US loan impairment charges rose by 85 per cent as delinquencies increased across much of the loan book. Part of the increase reflected the continued seasoning of the 2005, 2006 and early 2007 portfolios. The first half of 2008 saw a further weakening in the US economy and house price declines accelerated, reducing the amount of equity available for refinancing. Credit market turmoil meant the secondary market for securitised loans remained closed. Consequently, customers continued to experience difficulties in refinancing their loans. Bankruptcy levels increased as a rise in unemployment and increased fuel and food costs added to the financial pressures facing customers. Although the vast majority of mortgage customers continued to meet their commitments, delinquencies rose and loss severities increased.

HSBC continued to act to mitigate, where appropriate, the effects of the housing market decline on customers. In the first half of 2008, in the consumer finance business some 34,000 loans with an aggregate balance of approximately US$5.1 billion were modified. On a selective basis, longer term modifications were offered, typically for either two or five years.

Loan impairment charges in the mortgage services business more than doubled to US$1.9 billion. Rising delinquencies were partly offset by a decline in lending balances as the portfolio moved further into run-off.

In the consumer lending business, loan impairment charges rose by 69 per cent to US$2.1 billion as market conditions deteriorated. The decline was most severe in first lien loans in those states most affected by the housing market downturn. In addition, in the first half of 2008

delinquencies increased markedly in those states experiencing significant rises in unemployment. In response, credit criteria were tightened and an additional 100 branches were closed in the first half of 2008.

At HSBC Bank USA, the credit quality of residential mortgages deteriorated in the Home Equity Line of Credit and Home Equity Loan portfolios, while prime first lien mortgages also experienced higher levels of delinquency.

Credit and private label card loan impairment charges rose by 58 per cent to US$2.3 billion due to higher levels of non-prime balances, portfolio seasoning, increased bankruptcy filings, and the deterioration in the economy. Strategic initiatives were implemented to mitigate deteriorating credit trends on cards, including increased collection capacity, closure of inactive accounts, reductions in credit limits, a tightened approval process and restricted balance transfer volumes.

Impairment charges on the personal non-credit card portfolio rose by 40 per cent to US$1.2 billion. The deterioration in credit quality was more pronounced in some regions driven by the weakening US economy, rising unemployment rates and higher levels of bankruptcy filings. Loan impairment charges at the vehicle finance business rose by 44 per cent to US$335 million as economic deterioration led to higher loan defaults, while reduced demand for used cars, particularly larger vehicles, led to higher losses when repossessed vehicles were sold at auction.

In Canada, loan impairment charges rose by 52 per cent to US$125 million due to deteriorating delinquency rates in private label cards and mortgages, within the consumer finance business particularly in Western Canada, as the credit environment became more challenging. Loan impairment charges in the Canadian retail bank rose by US$9 million, largely driven by the vehicle finance business as a result of portfolio seasoning and higher fuel prices.

Operating expenses increased by 3 per cent to US$3.9 billion because of the goodwill impairment. Excluding this, costs declined. In the US, the management actions in 2007 to close the Decision One mortgage brokerage unit, cease correspondent acquisitions and reduce the consumer lending branch network led to a decline in staff costs. In addition, costs fell due to staff cuts from the reduction in size of the vehicle finance business and ongoing global cost reduction campaigns in processing and support functions. Other operating expenses declined as marketing on credit and private

label cards was curtailed to limit growth in loan balances. Branch closures in the consumer finance business and reduced mortgage services activity also led to lower operating costs. At the US retail bank, a rise in staff and other operating costs reflected increased investment in branch expansion and higher federal deposit insurance expenses. These costs were more than offset by the release of a litigation provision relating to a legal settlement prior to the Visa IPO in the second half of 2007.

Operating expenses rose by 5 per cent in Canada. Staff costs rose by a percentage point due to increased headcount in the Canadian retail bank following expansion in the branch network, which was partly offset by lower costs in consumer finance as a result of reduced headcount following branch closures in 2007 and the sale of a mortgage brokerage business in 2008. Other administrative and support costs rose, as investments made in the business, including expanding the branch network and online banking resulted in higher premises and depreciation costs.

Commercial Banking pre-tax profit declined by 15 per cent to US$430 million as loan impairment charges rose in the deteriorating economic environment.

Revenue increased, lifted by asset sales from HSBC Finance and fee income in Canada, partly offset by a fall in net interest income due to tighter spreads on deposits.

In the US, profit before tax fell by 22 per cent, with performance driven by tighter deposit spreads and increased loan impairment charges.

In Canada, profit before tax fell by 6 per cent to US$237 million as increased fee income was more than offset by higher loan impairment charges due to increased delinquency rates in the export and manufacturing sectors as a result of the slowing US economy, higher energy costs and a stronger Canadian dollar.

In Bermuda, profit before tax declined by 29 per cent due to lower net interest income as deposit spreads tightened following base rate cuts, and higher costs.

Net interest income declined by 2 per cent. In the US, net interest income fell by 3 per cent, as tighter deposit spreads in the declining rate environment more than offset a rise in deposit and loan volumes. The US retail bank continued its strategy of balancing growth between its established business in New York State and its expansion in the West Coast, Chicago and the Southeast. Average

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deposit balances rose by 11 per cent and loan balances increased by 11 per cent.

In the US, average loan balances to the middle market segment rose by 29 per cent to US$8.1 billion, outpacing the small business segment, where loans rose by 4 per cent in the face of increased competitive pressures. Management action led to a 3 per cent decline in commercial real estate activity compared with the first half of 2007, with increased repayments and reduced replacement business as the US retail bank took the opportunity to manage down lending exposures due to lower risk appetite and a deterioration in market conditions. Lending spreads widened on small business loans due to lower funding costs, but this was more than offset by tighter spreads on middle market and commercial real estate loans as yields declined due to a move towards higher credit quality customers, although spreads improved markedly in the second quarter.

Average deposit balances with small businesses in the US rose by 8 per cent to US$13 billion, due to strong growth in markets outside New York. Middle market deposits rose 23 per cent while commercial real estate deposit growth was subdued due to the exiting from selected associated lending relationships. The rise in balances was more than offset by narrower deposit spreads in the declining rate environment and competitive pricing pressures.

In Canada, net interest income was broadly in line with the first half of 2007 at US$337 million, as balance sheet growth offset tightening lending spreads. Average deposit balances rose by 8 per cent due to higher cash management balances, driven by an increase in account numbers following an expansion of the product offering. Deposit spreads remained constant as deposit rates and yields on surplus funds were unchanged despite lower base rates as credit spreads widened.

Average lending balances rose by 13 per cent, driven by lending growth, particularly in floating rate products, in the buoyant Western Canada region. Elsewhere, lending growth was experienced across all regions as the economy remained robust. Lending spreads tightened as interest rate cuts were immediately passed on to floating rate borrowers, in contrast to the wholesale cost of funding, which was adversely affected by wider credit spreads.

In Bermuda, net interest income decreased by 19 per cent, driven by tighter deposit spreads on current accounts as base rates declined. Average deposit balances rose by 23 per cent, reflecting continued strong demand from the insurance and construction sectors.

Net fee income rose by 20 per cent. In the US, fees increased by 7 per cent due to higher deposit service charges as a result of the successful expansion of cash management product offerings, higher debit card fees and increased loan syndication and agency fees for commercial real estate. In Canada, fee income rose by 36 per cent, driven by an increase in revenue as volumes of trade related money market instruments rose and higher fund transfer commissions as client activity increased.

Other operating income was higher due to increased gains from sales of assets in the legacy HSBC Finance commercial portfolio.

In the US, *loan impairment charges* more than doubled to US$106 million as the deteriorating economic outlook and customer downgrades prompted an increase in impairment allowances in the middle market and commercial real estate portfolios, as well as higher impairment charges for small business loans. While impairment allowances in middle market and commercial real estate increased, the level of write-offs on these portfolios improved, resulting in a small level of recoveries.

Loan impairment charges in Canada rose by US$38 million from the low levels reported in 2007 due to asset growth and higher delinquency rates in the manufacturing and export sectors, the result of the slowing US economy, higher energy costs and stronger Canadian dollar.

Operating expenses in the US were broadly unchanged as a decline in staff costs was offset by a rise in branch network-related costs. Staff costs fell due to lower incentive compensation and a decrease in headcount due to the consolidation of lending support functions. Administrative expenses rose by 9 per cent, mainly due to marketing spend.

Operating expenses in Canada were in line with the first half of 2007. Staff costs were broadly unchanged as higher salaries and benefits from growth in headcount due to continued investment in the business were offset by lower performance related pay. Other operating expenses fell due to lower capital taxes.

Global Banking and Markets reported a loss before tax of US$1.6 billion, compared with a profit of US$436 million in the first half of 2007. The disruption in global credit markets led to US$2.3 billion of write-downs in Credit and structured credit trading exposures and in monoline exposures and leveraged loans. Aside from these write-downs, pre-tax profit grew compared with the first half of 2007, as the performance of other trading

businesses improved and net interest income and net fee income increased.

Total operating losses of US$843 million were driven by the write-downs noted above. These losses were partly mitigated by increased income in other trading product areas, and in Balance Sheet Management.

Net interest income increased by 58 per cent as Balance Sheet Management benefited from the falling short-term US interest rates. Strong deposit balance growth in payments and cash management also contributed.

Net fee income rose by 31 per cent. Global Asset Management benefited from the market turmoil as institutional clients moved assets into less volatile cash funds. Advisory fee income also rose in capital markets, chiefly due to earnings from the Visa IPO.

Trading losses of US$1.7 billion were primarily driven by the write-downs noted above. Due to the credit market turmoil, the fair value of credit instruments such as mortgage loans and structured credit instruments deteriorated as the credit and liquidity disruption that began in the US sub-prime market spread into other mortgage and mortgage-related products. Trading in new US mortgages and related products was discontinued in late 2007. HSBC transacts with monoline insurers to buy protection against losses from defaults, primarily on credit products. For a description of the background to monoline write-downs, see page 36. The market turmoil also caused the market value of some leveraged and acquisition finance loans to fall due to general credit and liquidity disruption. More information on these write-downs and the underlying assets is available on page 113.

Other trading product areas continued to perform strongly, including foreign exchange and Rates, up by 99 per cent and 355 per cent, respectively, compared with the same period in 2007. Rates trading benefited from reduced market liquidity, which provided opportunities for wider spreads, and from increased market volatility. Foreign exchange trading income increased on higher customer trading and a strengthening of major currencies against the US dollar. Metals trading revenues benefited from higher prices in gold and platinum. Income from the equities business grew from increased customer trading volumes, which were driven by equity market volatility, and through capital markets fees.

Market conditions led to lower Principal Investments activity, resulting in a decline in *Other operating income*, and *Gains less losses from financial investments* fell as income from the disposal of securities declined.

Loan impairment charges rose because of weaker credit fundamentals which have resulted in a higher number of downgrades, particularly in comparison with the releases in the first half of 2007.

Operating expenses fell due to a 7 per cent reduction in staff numbers following the restructuring of a number of businesses during the second half of 2007 and first half of 2008 in response to market conditions. This included the closure of the mortgage-backed securities business in the US. The financial performance also led to lower performance-related costs, which further reduced operating expenses.

Private Banking reported a pre-tax profit of US$58 million in line with the first half of 2007, as unchanged revenues were offset by increased operating expenses. The cost efficiency ratio worsened by 4.8 percentage points to 74.2 per cent, with a number of new hires in the US and Canada.

Net interest income decreased by 5 per cent to US$112 million. Higher volumes of domestic savings and foreign time deposit accounts were driven by clients moving their assets under management to safer cash products, and new client relationships. However, this was offset by compressed spreads in the US due to a reduction in short-term US dollar interest rates.

Other revenues grew 5 per cent to US$117 million, driven mainly by an 11 per cent increase in *net fee income*. In the US, improved revenue sharing between customer groups led to increased asset management and custody fees and higher brokerage income. In Bermuda, HSBC also reported a rise in fee income, benefiting from improved brokerage and trust income fees, with the introduction of new tariffs.

Client assets increased by 1 per cent to US$58.8 billion compared with 31 December 2007, primarily in domestic custody and trust accounts, with net new money of US$1.4 billion offset by negative market movements.

Operating expenses were 7 per cent higher at US$170 million. A 7 per cent rise in staff costs was due to increased headcount relating to business expansion.

Within **Other**, profit before tax of US$294 million was reported compared with a loss of US$26 million in the first half of 2007.

Fair value movements on HSBC s own debt resulted in gains of US$354 million, primarily due to

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the widening credit spreads in the first quarter. Costs at HSBC.com and HSBC Technology USA Inc, the providers of technology services in North America,

decreased by 3 per cent to US$696 million. Related recharges are reported in other operating income.

Reconciliation of reported and underlying profit before tax

Half-year to 30 June 2008 (1H08) compared with half-year to 31 December 2007 (2H07)

North America	2H07 as reported US$m	Disposals and dilution gains[1] US$m	Currency translation[2] US$m	2H07 at 1H08 exchange rates US$m	Acquisitions[1] US$m	Underlying change US$m	1H08 as reported US$m	Reported change %	Underlying change %
Net interest income	7,540		3	7,543		330	7,873	4	4
Net fee income	2,906	(52)	1	2,855		(33)	2,822	(3)	(1)
Other income/(expense)[3]	857	(18)	1	840		(1,936)	(1,096)	(228)	(230)
Net operating income[4]	11,303	(70)	5	11,238		(1,639)	9,599	(15)	(15)
Loan impairment charges and other credit risk provisions	(8,336)		2	(8,334)		1,168	(7,166)	14	14
Net operating income	2,967	(70)	7	2,904		(471)	2,433	(18)	(16)
Operating expenses	(5,321)	48	(3)	(5,276)		(58)	(5,334)		(1)
Operating loss	(2,354)	(22)	4	(2,372)		(529)	(2,901)	(23)	(22)
Income from associates	10			10		(2)	8	(20)	(20)
Loss before tax	(2,344)	(22)	4	(2,362)		(531)	(2,893)	(23)	(22)

For footnotes, see page 89.

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Interim Management Report: Business Review (continued)

Analysis by customer group and global business

Profit/(loss) before tax

	Half-year to 30 June 2008						
North America	**Personal Financial Services US$m**	**Commercial Banking US$m**	**Global Banking and Markets US$m**	**Private Banking US$m**	**Other US$m**	**Inter-segment elimination[9] US$m**	**Total US$m**
Net interest income	**6,609**	**758**	**330**	**112**	**209**	**(145)**	**7,873**
Net fee income/(expense)	**2,145**	**192**	**426**	**98**	**(39)**		**2,822**
Trading income/(expense) excluding net interest income	**(51)**	**4**	**(2,001)**	**11**	**(154)**		**(2,191)**
Net interest income/(expense) on trading activities	**35**		**292**		**(97)**	**145**	**375**
Net trading income/(expense)[7]	**(16)**	**4**	**(1,709)**	**11**	**(251)**	**145**	**(1,816)**
Net income from financial instruments designated at fair value	**4**	**2**	**7**	**1**	**354**		**368**
Gains less losses from financial investments	**105**	**3**	**(4)**		**2**		**106**
Dividend income	**8**		**31**		**1**		**40**
Net earned insurance premiums	**203**						**203**
Other operating income/(expense)	**(100)**	**88**	**76**	**7**	**715**	**(671)**	**115**
Total operating income/(expense)	**8,958**	**1,047**	**(843)**	**229**	**991**	**(671)**	**9,711**
Net insurance claims[8]	**(112)**						**(112)**
Net operating income[4]/(expense)	**8,846**	**1,047**	**(843)**	**229**	**991**	**(671)**	**9,599**
Loan impairment charges and other credit risk provisions	**(6,952)**	**(156)**	**(57)**	**(1)**			**(7,166)**
Net operating income/(expense)	**1,894**	**891**	**(900)**	**228**	**991**	**(671)**	**2,433**
Total operating expenses	**(3,944)**	**(468)**	**(725)**	**(170)**	**(698)**	**671**	**(5,334)**
Operating profit/(loss)	**(2,050)**	**423**	**(1,625)**	**58**	**293**		**(2,901)**
Share of profit in associates and joint ventures		**7**			**1**		**8**
Profit/(loss) before tax	**(2,050)**	**430**	**(1,625)**	**58**	**294**		**(2,893)**

	%	**%**	**%**	**%**	**%**	**%**
Share of HSBC s profit before tax	**(20.0)**	**4.2**	**(15.9)**	**0.6**	**2.9**	**(28.2)**
Cost efficiency ratio	**44.6**	**44.7**	**(86.0)**	**74.2**	**70.4**	**55.6**
Balance sheet data[6]						
	US$m	**US$m**	**US$m**	**US$m**	**US$m**	**US$m**
Loans and advances to customers (net)	**201,941**	**37,756**	**27,137**	**5,656**		**272,490**
Total assets	**236,672**	**44,023**	**243,132**	**6,846**	**934**	**531,607**
Customer accounts	**66,281**	**36,881**	**23,709**	**15,020**	**109**	**142,000**
Loans and advances to banks (net)[12]			**18,624**			
Trading assets[12,13]			**158,218**			
Financial instruments designated at fair value[12]						
Financial investments[12]			**35,902**			
Deposits by banks[12]			**10,909**			
Trading liabilities[12,13]			**152,093**			

For footnotes, see page 89.

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Profit/(loss) before tax

	Half-year to 30 June 2007						
North America	Personal Financial Services US$m	Commercial Banking US$m	Global Banking and Markets US$m	Private Banking US$m	Other US$m	Inter-segment elimination[9] US$m	Total 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 net interest income	(184)	3	483	6	(62)		246
Net interest income on trading activities	87		10			279	376
Net trading income/(expense)[7]	(97)	3	493	6	(62)	279	622
Net income from financial instruments designated at fair value			3		78		81
Gains less losses from financial 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
Total operating income	9,169	954	1,197	279	693	(688)	11,604
Net insurance claims[8]	(124)						(124)
Net operating income[4]	9,045	954	1,197	279	693	(688)	11,480
Loan impairment (charges)/recoveries and other credit risk provisions	(3,774)	(46)	12	(12)			(3,820)
Net operating income	5,271	908	1,209	267	693	(688)	7,660
Total operating expenses	(3,783)	(443)	(771)	(207)	(719)	688	(5,235)
Operating profit/(loss)	1,488	465	438	60	(26)		2,425
Share of profit/(loss) in associates and joint ventures		12	(2)				10
Profit/(loss) before tax	1,488	477	436	60	(26)		2,435
	%	%	%	%	%		%
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[6]

	US$m	US$m	US$m	US$m	US$m		US$m
	219,735	34,831	21,462	5,267			281,295

Loans and advances to customers (net)							
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)[12]			16,289				
Trading assets[12,13]			146,387				
Financial instruments designated at fair value[12]							
Financial investments[12]			33,790				
Deposits by banks[12]			10,927				
Trading liabilities[12,13]			131,111				

For footnotes, see page 89.

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Interim Management Report: Business Review (continued)

Analysis by customer group and global business *(continued)*

Profit/(loss) before tax

	Half-year to 31 December 2007						
North America	Personal Financial Services US$m	Commercial Banking US$m	Global Banking and Markets US$m	Private Banking US$m	Other US$m	Inter-segment elimination[9] US$m	Total US$m
Net interest income	6,630	818	176	156	1	(241)	7,540
Net fee income/(expense)	2,239	186	381	139	(39)		2,906
Trading income/(expense) excluding net interest income	(165)	(5)	(1,354)	5	(16)		(1,535)
Net interest income/(expense) on trading activities	47		127		(44)	241	371
Net trading income/(expense)[7]	(118)	(5)	(1,227)	5	(60)	241	(1,164)
Net expense from financial instruments designated at fair value			8		1,661		1,669
Gains less losses from financial investments	167	(1)	23		3		192
Dividend income	12		29				41
Net earned insurance premiums	218						218
Other operating income/(expense)	(119)	30	58	20	745	(716)	18
Total operating income	9,029	1,028	(552)	320	2,311	(716)	11,420
Net insurance claims[8]	(117)						(117)
Net operating income/(expense)[4]	8,912	1,028	(552)	320	2,311	(716)	11,303
Loan impairment (charges)/recoveries and other credit risk provisions	(8,135)	(145)	(58)	2			(8,336)
Net operating income/(expense)	777	883	(610)	322	2,311	(716)	2,967
Total operating expenses	(3,811)	(450)	(791)	(208)	(777)	716	(5,321)
Operating profit/(loss)	(3,034)	433	(1,401)	114	1,534		(2,354)
Share of profit in associates and joint ventures		10					10
Profit/(loss) before tax	(3,034)	443	(1,401)	114	1,534		(2,344)

	%	%	%	%	%		%
Share of HSBC s profit before tax	(30.2)	4.4	(13.9)	1.1	15.3		(23.3)
Cost efficiency ratio	42.8	43.8	143.3	65.0	33.6		47.1
Balance sheet data[6]							
	US$m	US$m	US$m	US$m	US$m		US$m
Loans and advances to customers (net)	218,676	38,930	26,186	6,068			289,860
Total assets	240,734	43,920	217,808	6,541	1,089		510,092
Customer accounts	61,824	36,306	30,732	16,187	124		145,173
Loans and advances to banks (net)[12]			14,938				
Trading assets[12,13]			149,926				
Financial instruments designated at fair value[12]							
Financial investments[12]			33,273				
Deposits by banks[12]			14,825				
Trading liabilities[12,13]			126,139				

For footnotes, see page 89.

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Latin America

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

	Personal Financial Services US$m	Commercial Banking US$m	Global Banking and Markets US$m	Private Banking US$m	Other US$m	Total US$m
Half-year to 30 June 2008						
Brazil	**262**	**200**	**193**	**6**	**(1)**	**660**
Mexico	**151**	**127**	**106**	**1**		**385**
Argentina	**21**	**43**	**55**			**119**
Panama	**31**	**18**	**13**	**1**		**63**
Other	**3**	**23**	**16**		**(3)**	**39**
	468	**411**	**383**	**8**	**(4)**	**1,266**
Half-year to 30 June 2007						
Brazil	101	116	141	4	(2)	360
Mexico	251	169	50	5		475
Argentina	10	33	49		3	95
Panama	17	11	10	1		39
Other	9	23	3		(4)	31
	388	352	253	10	(3)	1,000
Half-year to 31 December 2007						
Brazil	192	170	156	5	(4)	519
Mexico	263	164	63	6	9	505
Argentina	26	42	41		(3)	106
Panama	28	7	6	6		47
Other	(4)	5	(2)	(2)	4	1
	505	388	264	15	6	1,178

Loans and advances to customers (net) by country

	At 30 June 2008 US$m	At 30 June 2007 US$m	At 31 December 2007 US$m
Brazil	**23,721**	14,104	18,491
Mexico	**18,557**	16,063	18,059
Argentina	**2,704**	2,026	2,485
Panama	**4,294**	4,059	4,158
Other	**4,976**	4,354	4,730

	54,252	40,606	47,923

Customer accounts by country

	At 30 June 2008 US$m	At 30 June 2007 US$m	At 31 December 2007 US$m
Brazil	**35,285**	23,660	26,231
Mexico	**22,562**	19,916	22,307
Argentina	**3,300**	2,659	2,779
Panama	**5,338**	4,678	5,062
Other	**5,294**	4,336	4,913
	71,779	55,249	61,292

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Interim Management Report: Business Review (continued)

Profit before tax

Latin America	30 June 2008 US$m	Half-year to 30 June 2007 US$m	31 December 2007 US$m
Net interest income	**3,362**	2,534	3,042
Net fee income	**1,139**	998	1,155
Net trading income	**358**	285	263
Net income from financial instruments designated at fair value	**156**	157	163
Gains less losses from financial investments	**168**	98	155
Gains arising from dilution of interests in associates			11
Dividend income	**6**	6	3
Net earned insurance premiums	**900**	731	863
Other operating income	**130**	153	75
Total operating income	**6,219**	4,962	5,730
Net insurance claims incurred and movement in liabilities to policyholders	**(764)**	(676)	(751)
Net operating income before loan impairment charges and other credit risk provisions	**5,455**	4,286	4,979
Loan impairment charges and other credit risk provisions	**(1,170)**	(775)	(922)
Net operating income	**4,285**	3,511	4,057
Total operating expenses	**(3,023)**	(2,516)	(2,886)
Operating profit	**1,262**	995	1,171
Share of profit in associates and joint ventures	**4**	5	7
Profit before tax	**1,266**	1,000	1,178
	%	%	%
Share of HSBC s profit before tax	**12.3**	7.1	11.7
Cost efficiency ratio	**55.4**	58.7	58.0
Period-end staff numbers (full-time equivalent)	**63,851**	66,875	64,404

Balance sheet data[6]

	US$m	US$m	US$m
Loans and advances to customers (net)	**54,252**	40,606	47,923
Loans and advances to banks (net)	**17,192**	13,345	12,675
Trading assets, financial instruments designated at fair value, and financial investments	**27,929**	22,107	24,715
Total assets	**117,019**	88,925	99,056

Deposits by banks	**4,705**	4,727	4,092
Customer accounts	**71,779**	55,249	61,292

For footnote, see page 89.

Economic briefing

Economic growth in **Mexico** moderated during the first half of 2008, partly in response to the slowdown in activity within the US. GDP rose by 2.6 per cent in the first quarter of the year on the equivalent period in 2007, compared with 3.3 per cent for the whole of 2007. Inflationary pressures intensified, with the headline rate of consumer price inflation experiencing sharp gains, rising from an annual rate of 3.8 per cent in December 2007 to 5.3 per cent in June 2008, mostly from higher food and energy prices. In response to these inflationary pressures,

the Bank of Mexico raised its overnight interest rate by 25 basis points in June 2008.

The **Brazilian** economy continued to expand strongly with first quarter GDP rising by 5.8 per cent year-on-year, driven by strong domestic demand and consumer spending. Conditions within the labour market continued to improve, supporting consumer confidence, with the rate of unemployment well below levels observed a year earlier. Inflation continued to accelerate, with the headline annual rate of consumer price inflation rising to 6.1 per cent in June 2008 from 4.5 per cent in December 2007. Rising food prices were the most prominent cause,

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but core inflation (excluding food and energy) also rose, reflecting buoyant domestic conditions. Rising import demand was also expected to trigger a deterioration in the current account position during 2008 as a whole. With inflation near the upper limit of the Central Bank of Brazil s tolerance range, a modest tightening of monetary policy was initiated and the Selic target rate was increased from 11.25 per cent in April 2008 to 12.25 per cent in June 2008.

Argentina s growth continued at a high level during the first quarter of the year, with overall GDP

rising by 8.4 per cent year-on-year compared with an average of 8.6 per cent for 2007 as a whole, even though industrial action within the agricultural sector is believed to have adversely affected activity levels during the period. Some further slowing of activity is expected to occur during the remainder of 2008 while inflationary pressures remain of concern. The reported headline rate of consumer price inflation rose from 8.5 per cent in December 2007 to 9.3 per cent in June 2008, although changes in methodologies make comparisons between the periods difficult.

Reconciliation of reported and underlying profit before tax

	Half-year to 30 June 2008 (1H08) compared with half-year to 30 June 2007 (1H07)								
Latin America	**1H07 as reported US$m**	**Disposals and dilution gains[1] US$m**	**Currency translation[2] US$m**	**1H07 at 1H08 exchange rates US$m**	**Acquisitions[1] US$m**	**Under-lying change US$m**	**1H08 as reported US$m**	**Re-ported change %**	**Under-lying change %**
Net interest income	**2,534**		**286**	**2,820**		**542**	**3,362**	**33**	**19**
Net fee income	**998**		**102**	**1,100**		**39**	**1,139**	**14**	**4**
Other income[3]	**754**		**82**	**836**		**118**	**954**	**27**	**14**
Net operating income[4]	**4,286**		**470**	**4,756**		**699**	**5,455**	**27**	**15**
Loan impairment charges and other credit risk provisions	**(775)**		**(97)**	**(872)**		**(298)**	**(1,170)**	**(51)**	**(34)**
Net operating income	**3,511**		**373**	**3,884**		**401**	**4,285**	**22**	**10**
Operating expenses	**(2,516)**		**(283)**	**(2,799)**		**(224)**	**(3,023)**	**(20)**	**(8)**
Operating profit	**995**		**90**	**1,085**		**177**	**1,262**	**27**	**16**
Income from associates	**5**			**5**		**(1)**	**4**	**(20)**	**(20)**
Profit before tax	**1,000**		**90**	**1,090**		**176**	**1,266**	**27**	**16**

For footnotes, see page 89.

Review of business performance

HSBC s operations in Latin America reported a pre-tax profit of US$1.3 billion compared with US$1.0 billion in the first half of 2007, representing an increase of 27 per cent.

During the first half of 2008, HSBC continued in its efforts to grow the business organically in Mexico and Brazil while integrating recently acquired businesses in Argentina and Central America. The Visa IPO resulted in gains on the redemption of shares held by the Group. Credit quality in maturing portfolios continued to be an area of focus for management, especially in the Personal Financial Services credit card business in Mexico. The Premier relaunch in 2007 resulted in an increase in customer numbers and income in the first six months of 2008. The insurance business s contribution to the performance of the region increased in the first half of 2008, largely due to growth in premiums, mainly on term life and motor

products, which exceeded expense growth. In Commercial Banking, HSBC continued in its strategy to be the leading international bank through its extended network of International Banking Centres, increased focus on trade finance and growth in referrals of international business opportunities. As part of HSBC s strategy to be the best bank for small businesses, Brazil introduced an initiative in the second half of 2007, called Empreendedor Direto with the aim of providing more focus on micro businesses. Global Banking and Markets benefited from favourable market conditions which increased revenues and from foreign exchange rate volatility which drove higher trading revenues.

On an underlying basis, pre-tax profits rose by 16 per cent. Increased revenues were partly offset by higher loan impairment charges, mainly driven by the cards business in Mexico, and increased operating costs across the region. The cost efficiency ratio improved by 3.4 percentage points to 55.4 per cent.

The following commentary is on an underlying basis.

Personal Financial Services reported a pre-tax profit of US$468 million, an 11 per cent increase on the first half of 2007. Growth in revenue was driven by continued organic balance sheet growth, especially in cards and personal loans in Mexico and vehicle finance and payrolls in Brazil. This was augmented by gains from the redemption of shares in the Visa IPO and interest on the recovery of transactional taxes paid in previous years in Brazil. Following the global relaunch of Premier in a number of countries in 2007, there were increases in both the number of Premier customers and the average income per customer in the region. The growth in balance sheet volumes in Mexico and Brazil, coupled with higher delinquency rates, drove an increase in loan impairment charges. Increased operating expenditure was partially offset by a recovery of transactional taxes in Brazil following a court ruling. The cost efficiency ratio improved by 4.7 percentage points as revenues grew faster than costs.

In Mexico, pre-tax profits decreased by 42 per cent, largely driven by higher loan impairment charges on credit cards and personal loans following balance sheet growth and increased delinquency. Net operating income before loan impairment charges rose by 17 per cent on higher interest generated by the growth in credit card balances and a gain on the redemption of Visa shares. Operating costs grew by 12 per cent.

In Brazil, profit before tax grew by 111 per cent on higher income driven by balance sheet growth, partially offset by a decrease in fee income due to regulatory changes. Profit before tax also benefited from the refinement of the income recognition methodology in respect of long-term insurance contracts and a gain on redemption of Visa shares. A recovery of transactional taxes paid in earlier years and interest thereon increased interest income and resulted in lower operating expenses.

In Argentina, profit before tax grew by 116 per cent. Balance sheet growth drove an increase in net interest income which was partly offset by higher costs and loan impairment charges.

Net interest income rose by 17 per cent to US$2,376 million.

In Mexico, net interest income rose by 26 per cent, driven by higher balance sheet volumes and improved spreads. Despite a slowdown in credit card

sales, average loan balances continued to grow. Average total loans grew by 12 percentage points. Spreads widened by 417 basis points on personal loans and by 316 basis points on credit cards due to re-pricing initiatives implemented during the second half of 2007.

Average demand deposit balances rose by 7 per cent. Average balances of time deposits grew by 14 per cent, driven by competitive pricing. HSBC s market share for deposits remained stable.

In Brazil, net interest rose by 9 per cent. A favourable economic scenario and increased household income drove higher consumption and demand for credit. As a result, vehicle finance loans increased by 39 per cent and payroll loans by 57 per cent. Average card balances grew by 25 per cent, following market growth and new deals on co-branded cards combined with marketing promotions to improve card usage. This was partially offset by a decrease of 3 per cent in personal instalment loans due to increased competition in the market.

Spreads widened on cards and overdrafts as a result of lower funding costs and repricing initiatives, in line with market trends, but narrowed on vehicle finance and payroll loans due to increased competition. Overall, spreads were lower, reflecting the business strategy of seeking reduced credit risk by focusing on secured loans.

Net interest income also increased as a result of a favourable court decision, which granted HSBC the right to recover transactional taxes paid in excess on insurance transactions, and interest accrued thereon.

In Argentina, net interest income grew by 69 per cent. Average loan volumes increased by 39 per cent as personal loans, credit cards and car loan balances all rose. These increases resulted from higher sales of pre-approved facilities, supported by a new credit policy for personal loans, and marketing campaigns. Spreads improved on car loans and overdrafts as a result of repricing initiatives. The overall spread on lending products narrowed by 28 basis points. The average term deposit portfolio increased by 11 per cent following several initiatives including improved incentives for staff in the branch network, the appointment of a number of Premier executives and the implementation of campaigns to support growth through the internet. The number of Premier customers increased by 30 per cent. The overall spread increased by 94 basis points.

Net fee income increased by 2 per cent to US$712 million, mainly in Mexico where fee income rose by 14 per cent. Credit card annual fees

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increased by 29 per cent, reflecting an increase of almost 35,000 in the number of cards in force. Collection fees and late-payment fees increased following the application of stricter guidelines in June 2007. Income from deposit accounts continued to rise, as a result of an increase in membership fees and the introduction of a flexible pricing option. Income from e-channels rose by 6 per cent on higher usage.

In Brazil, fee income fell by 15 per cent, following a ruling by the Brazilian Central Bank removing certain fees, such as charges on early loan repayments and returned cheques. The effect was compounded by a lower number of transactions, which reduced current account fees, and the discontinuation of commission paid by the Brazilian social security agency for pension payment services. This was partly offset by a rise in pension administration fees and higher cards income driven by growth in cards in force.

In Argentina, net fee income decreased by 18 per cent, mainly because lower commissions were earned from the pension fund business following pension-related reform introduced by the government. Higher general insurance sales resulted in increased commissions paid. This was partially offset by higher commission income on vehicle loans and credit cards, reflecting volume growth.

Gains from financial investments increased by US$74 million, mainly because of a gain on redemption of Visa shares following the global IPO. Gains were recorded in Mexico (US$55 million), Panama (US$12 million), Brazil (US$11 million) and other Central American countries (US$5 million). Brazil also recorded a gain of US$16 million on the sale of shares in a local stock exchange. A gain of US$33 million on a similar sale of shares was registered in the first half of 2007.

Other operating income fell, mainly because, in the first half of 2007, results benefited from a one-off refinement of the income recognition methodology used in respect of long-term insurance contracts in Mexico. This was partially offset by a similar adjustment in Brazil in the first half of 2008 which resulted in a non-recurrent gain of US$45 million.

Net insurance premiums rose by 8 per cent to US$802 million. In Mexico, growth of 20 per cent was mainly driven by higher gross premiums on life and motor products. Sales of life products grew faster than non-life products due to an increased focus by HSBC on life insurance sales through the branch network and other distribution channels, in particular, the telemarketing of personal accident

insurance. In Brazil, net insurance premiums rose by 9 per cent. Pension-related business grew, driven by sales initiatives which generated organic growth in both regular and additional contributions.

In Argentina, insurance premium growth was driven by the general insurance business from a mixture of higher premiums and increased sales. Vehicle insurance products generated the largest increases, mainly because of higher prices. Overall, premium income on life insurance decreased due to the cessation of part of the business related to the pension fund portfolio as a consequence of changes in government legislation.

Loan impairment charges rose by 35 per cent, to US$1.1 billion. In Mexico, loan impairment charges rose by 76 per cent, largely from portfolio growth and higher delinquency in the credit card portfolio following HSBC s targeted expansion in the market in previous years. The increase in loan impairment charges is a cost of building higher market share through organic growth in an area where HSBC was previously under-represented. Personal instalment loans also contributed to the increase in loan impairment charges.

Loan impairment charges in Brazil rose by 8 per cent, reflecting strong asset growth and higher delinquency levels in vehicle finance, and store loans which were partly offset by the gain on sale of an impaired loan portfolio. The impaired loan to total customer loans ratio, improved by 1.2 percentage points. Credit models were updated during the first half of 2008 to reflect recent underwriting experience and were supplemented by improved collection strategies.

In Argentina, growth in loan impairment charges of 68 per cent was driven by increased customer advances and higher delinquency levels on the consumer finance portfolio.

Operating expenses increased by 5 per cent to US$2.1 billion.

In Mexico, operating expenses grew by 12 per cent. Staff costs rose as a result of the annual salary review in earlier 2008, partly offset by lower staff numbers. Non-staff costs rose on the increased use of the cash-back facility on the Tu Cuenta product. This was partly offset by a decrease in contract personnel as a result of a refinement in asset growth strategy in the latter part of 2007.

In Brazil, expenses decreased by 5 per cent, as a result of the recognition of a tax credit related to a court decision granting the right to recover excess taxes paid on insurance transactions. Transactional taxes reduced further, due to the removal of tax on

withdrawals in 2008. Additional costs were incurred in support of growth in the credit card business and improved operational processes for both debit and credit cards. Staff costs increased marginally, mainly driven by increased performance-related incentives, in line with profit growth and union-agreed pay rises. This increase was partially offset by a restructuring exercise initiated in the first half of 2007 which reduced staff numbers.

In Argentina, expenses grew by 29 per cent. Staff costs rose on higher salaries following pay reviews. Non-staff costs increased in the form of utility and general administration costs due to higher prices following inflation adjustments by suppliers.

Commercial Banking reported pre-tax profits of US$411 million, an increase of 8 per cent over the first half of 2007. Revenues grew as the business continued to expand in the region in line with HSBC s objective to be the leading international bank and the best bank for small businesses. The regional network of International Banking Centres based in Argentina, Brazil and Mexico significantly increased their number of successful international referrals. Loan impairment charges rose by 26 per cent. Operating expenses increased by 11 per cent. The cost efficiency ratio improved by 0.2 percentage points.

In Mexico, a decline in profit before tax of 27 per cent was mainly the result of a one-off writeback of loan impairment charges in 2007, following a review of credit models.

In Brazil, pre-tax profits rose by 44 per cent, driven by higher net interest income on strong balance sheet growth and lower loan impairment charges as delinquency levels improved.

In Argentina, profit before tax rose by 33 per cent, as net interest and fee income rose on business growth.

Net interest income increased by 10 per cent to US$800 million, mainly as a result of balance sheet growth.

In Mexico, net interest income rose by 2 per cent on increased volumes in medium-sized business loans, in both local currency and US dollars, and real estate loans, which were driven by market growth in the construction sector. Loans denominated in US dollars rose due to higher demand as a result of the lower dollar rates. The spread for small and medium business loans widened following a repricing strategy. US dollar denominated loan spreads narrowed by 137 basis points due to higher funding costs.

Average balances on total deposits increased by 18 per cent as customers held higher balances for longer periods. Regulations prohibiting government treasuries from holding balances in non-interest bearing accounts resulted in a shift in commercial balances from demand to term deposits, putting pressure on the overall yield. Spreads on deposits denominated in US dollars narrowed in a falling rate environment.

In Brazil, the favourable economic scenario led to an increase in the demand for credit. Sales and repricing initiatives, combined with longer loan maturity periods and improved geographical coverage, contributed to robust growth in lending balances and an increase in net interest income of 15 per cent. The strong growth was mostly in working capital, receivables-backed loans and trade finance. Spreads were slightly lower in the overall portfolio as a consequence of market competition and HSBC s business strategy of seeking reduced credit risk and focusing on secured loans and trade products. Spreads on overdrafts increased driven by a decline in base rates.

Sales through direct channels grew by 76 per cent, mostly in guaranteed accounts, discounted trade notes and investments. This was primarily driven by the launch of Empreendedor Direto in the second half of 2007.

In Argentina, net interest income grew by 49 per cent. Growth in both assets and liabilities was mainly driven by customer acquisitions following wider geographical coverage from the integration of Banca Nazionale del Lavoro SpA s commercial network. Overdraft balances grew on increased economic activity. Higher volumes of receivables finance were driven by focused marketing campaigns. The leasing portfolio grew by 40 per cent. Spreads on overdrafts widened, while spreads on receivables finance and leasing decreased.

Demand deposits grew by 22 per cent and term deposits grew by 9 per cent following a three month marketing campaign in 2008. Spreads in demand deposits widened on higher base rates but were partially offset by slightly lower spreads on term deposits due to a more competitive market environment. Overall, spreads on customer deposits widened by 133 basis points.

Net fee income was 5 per cent higher at US$271 million. In Brazil, this largely arose from increases in collection bill fees, mainly due to higher transaction volumes and repricing initiatives to align with local market prices. Standby letters of credit, bank guarantees and assets under management also contributed to this increase, driven by higher

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volumes as the business focused on cross-sales using customer relationship management tools. These tools enabled relationship managers to offer suitable products to customers which were more in line with their particular banking preferences.

In Mexico, fee income decreased by 3 per cent. Increased usage by non-HSBC customers following the recent extension of the network drove an increase of 76 per cent in automated teller machine (ATM) fees. Higher prices resulted in income growth on payments and cash management. These factors were offset by lower income on remittances, which fell in line with decreased volumes in the more competitive environment, coupled with the effects of the weakening US economy.

Higher fee income in Argentina was mainly due to increased account services commissions on greater customer activity and repricing of fees.

Trading income rose by 85 per cent to US$37 million, mainly in Brazil due to higher volumes of treasury products and spot foreign exchange deals which benefited from increased demand in the favourable economic conditions.

Loan impairment charges increased by 26 per cent to US$110 million due to higher loan impairment charges in Mexico, partially offset by lower ones Brazil.

In Mexico, higher loan impairment charges on commercial and real estate loans were mainly driven by organic growth in the portfolio. In 2007, net releases of loan allowances were reported in Mexico due to changes made to the credit models to more accurately represent the most recent behaviour in the underlying commercial loan portfolios. The risk profile of the loan portfolio remained stable during the first half of 2008.

In Brazil, loan impairment charges decreased by 18 per cent despite a 38 per cent growth in average lending balances. This was driven by improved delinquency levels in the small and medium enterprises segment and the absence of any new significant individual loan impairment charges in the current period.

Operating expenses increased by 11 per cent to US$643 million.

In Mexico, operating expenses increased by 10 per cent. Staff costs decreased as the effects of the annual salary review and higher performance-related compensation were offset by refinements in the allocation of statutory profit sharing compensation. Other operating expenses increased, primarily driven by higher operational losses.

Operating expenses in Brazil rose by 9 per cent. Staff costs grew as a result of higher remuneration and performance-related incentives aligned with business growth, and union-agreed pay rises. These factors were partly offset by lower headcount following business restructuring, resulting in increased efficiency. Other operating costs also grew due to higher litigation expenses, mainly driven by civil claims, and transactional taxes increased on higher volumes.

In Argentina, expenses increased by 65 per cent, mainly driven by higher indirect costs. Staff costs rose on following pay reviews in line with labour union agreements. Other costs also grew in the inflationary environment.

Global Banking and Markets reported a pre-tax profit of US$383 million, representing an increase of 36 per cent compared with the first half of 2007. In Mexico, pre-tax profits increased by 100 per cent, mainly as a result of higher net interest income. In Brazil, pre-tax profits grew by 12 per cent due to higher foreign exchange trading revenues. In Argentina, growth was driven by an increase in net interest income and foreign exchange trading income. The cost efficiency ratio for the region improved by 0.5 percentage points.

Total operating income rose by 33 per cent to US$726 million, mainly due to growth in foreign exchange trading in Brazil, reflecting the success of HSBC s strategy to provide a wider product range with a focus on structured derivatives, particularly to Commercial Banking customers, and due to an increase in income earned in Balance Sheet Management.

In Mexico, pre-tax profits increased due to strong growth in net interest income as favourable market conditions led to a robust performance from Balance Sheet Management. Trading income declined, despite growth in foreign exchange, as the Mexican financial markets continued to exhibit low levels of volatility.

In Brazil, pre-tax profits were 12 per cent higher, due to strong growth in foreign exchange trading and an increase in securities services deposits as clients moved funds into Brazil for investment. A significant increase in operating expenses was due to an investment in new IT systems to support volume growth as well as growth in staff numbers as HSBC enhanced its capabilities, including the establishment of a new global research team.

In Argentina, pre-tax profits improved by 14 per cent. Higher revenues were driven by growth in net interest income and an increase in foreign exchange trading income due to market volatility. This was partly offset by higher operating expenses, driven by high levels of inflation, an increase in staff costs following labour union agreements.

Net interest income rose by 68 per cent to US$337 million, predominantly from growth in Mexico. Balance Sheet Management performed well, driven by favourable market conditions in Mexico and Argentina, due to an increase in balance sheet volumes and wider spreads. In addition, the strong equity markets in Brazil led to an increase in securities services deposits as clients moved funds into the country for investment.

Net fee income grew by 5 per cent to US$131 million, largely in Mexico where increased loan facility fees were driven by higher lending volumes. Fee income increased in securities services, partly in Brazil, as a result of the increase in deposits discussed above. The development of the retail equity trading platform in Brazil also contributed to the increase in fee income.
Trading income was 29 per cent higher at US$137 million, driven by solid growth in foreign exchange trading in Brazil, due to a wider product offering which was particularly targeted at Commercial Banking customers. In Mexico, trading income declined, despite growth in foreign exchange, as the Mexican financial markets continued to exhibit low volatility, resulting in challenging trading conditions. Trading income in Argentina increased as a result of strong performance in foreign exchange in the volatile markets.

Gains less losses from financial investments decreased by 25 per cent to US$45 million, due to a lower value of disposals in Mexico, Brazil and Argentina compared with the first half of 2007.

A small release of *loan impairment charges* was in line with the first half of 2007.

Operating expenses increased by 33 per cent to US$309 million. A significant rise in operating expenses in Brazil was partly caused by higher IT costs due to investment in new systems to support volume growth and automate processes on complex products. Staff numbers increased in Global Markets, as HSBC enhanced its customer proposition, including the establishment of a new global research team. Performance costs also rose in line with improved performance in Global Markets. Operating expenses in Argentina increased, mainly driven by an increase in staff costs following a labour union pay agreement. Other costs grew in the inflationary environment.

Private Banking reported a pre-tax profit of US$8 million, a decrease of 20 per cent. An improved performance in Brazil was offset by higher expenditure in the region. As a result, the cost efficiency ratio worsened by 9.6 percentage points to 78.4 per cent.

Revenues grew by 16 per cent to US$37 million, with improvements in both net interest income and fee income. Balance sheet growth across the region drove the 44 per cent increase in *net interest income*, while improvements in securities trading in Brazil underpinned the rise in *net fee income*. This was offset by lower brokerage fees in Mexico, however, due to a general slowdown in the market.

Client assets were US$12.6 billion, compared with US$11.6 billion at 31 December 2007, due to new product offerings in Brazil. Inward referrals from other customer groups contributed US$444 million to total client assets, flat when compared with the first half of 2007.

Operating expenses grew by 32 per cent to US$29 million, driven by a rise in staff costs to support business expansion and increased bonuses.

Amounts reported in **Other** were largely in line with the first half of 2007.

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Reconciliation of reported and underlying profit before tax

Latin America	2H07 as reported US$m	Disposals and dilution gains[1] US$m	Currency translation[2] US$m	2H07 at 1H08 exchange rates US$m	Acqui-sitions[1] US$m	Under-lying change US$m	1H08 as reported US$m	Re-ported change %	Under-lying change %
	Half-year to 30 June 2008 (1H08) compared with half-year to 31 December 2007 (2H07)								
Net interest income	3,042		170	3,212		150	3,362	11	5
Net fee income	1,155		60	1,215		(76)	1,139	(1)	(6)
Other income[3]	782	(11)	43	814		140	954	22	17
Net operating income[4]	4,979	(11)	273	5,241		214	5,455	10	4
Loan impairment charges and other credit risk provisions	(922)		(49)	(971)		(199)	(1,170)	(27)	(20)
Net operating income	4,057	(11)	224	4,270		15	4,285	6	0
Operating expenses	(2,886)		(164)	(3,050)		27	(3,023)	(5)	1
Operating profit	1,171	(11)	60	1,220		42	1,262	8	3
Income from associates	7		(1)	6		(2)	4	(43)	(33)
Profit before tax	1,178	(11)	59	1,226		40	1,266	7	3

For footnotes, see page 89.

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Analysis by customer group and global business

Profit/(loss) before tax

	Half-year to 30 June 2008						
Latin America	**Personal Financial Services US$m**	**Commercial Banking US$m**	**Global Banking and Markets US$m**	**Private Banking US$m**	**Other US$m**	**Inter-segment elimination[9] US$m**	**Total US$m**
Net interest income/(expense)	2,376	800	337	13	(2)	(162)	3,362
Net fee income	712	271	131	19	6		1,139
Trading income excluding net interest income	16	34	130	1	1		182
Net interest income on trading activities	4	3	7			162	176
Net trading income[7]	20	37	137	1	1	162	358
Net income/(expense) from financial instruments designated at fair value	162		(6)				156
Gains less losses from financial investments	111	11	45	2	(1)		168
Dividend income	4		2				6
Net earned insurance premiums	802	47	56		(5)		900
Other operating income	98	20	24	2	7	(21)	130
Total operating income	4,285	1,186	726	37	6	(21)	6,219
Net insurance claims[8]	(706)	(22)	(36)				(764)
Net operating income[4]	3,579	1,164	690	37	6	(21)	5,455
Loan impairment (charges)/recoveries and other credit risk provisions	(1,060)	(110)	2		(2)		(1,170)
Net operating income	2,519	1,054	692	37	4	(21)	4,285
Total operating expenses	(2,055)	(643)	(309)	(29)	(8)	21	(3,023)
Operating profit/(loss)	464	411	383	8	(4)		1,262
Share of profit in associates and joint ventures	4						4
Profit/(loss) before tax	468	411	383	8	(4)		1,266
	%	%	%	%	%		%

Share of HSBC s profit before tax	**4.6**	**4.0**	**3.7**	**0.1**	**(0.1)**	**12.3**
Cost efficiency ratio	**57.4**	**55.2**	**44.8**	**78.4**	**133.3**	**55.4**

Balance sheet data[6]

	US$m	US$m	US$m	US$m	US$m	US$m
Loans and advances to customers (net)	**24,431**	**19,073**	**10,704**	**44**		**54,252**
Total assets	**39,883**	**24,505**	**52,290**	**300**	**41**	**117,019**
Customer accounts	**34,368**	**17,021**	**19,072**	**1,318**		**71,779**
Loans and advances to banks (net)[12]			**13,812**			
Trading assets[12,13]			**12,303**			
Financial instruments designated at fair value[12]			**106**			
Financial investments[12]			**11,781**			
Deposits by banks[12]			**2,812**			
Trading liabilities[12,13]			**7,878**			

For footnotes, see page 89.

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Profit/(loss) before tax

	Half-year to 30 June 2007						
Latin America	Personal Financial Services US$m	Commercial Banking US$m	Global Banking and Markets US$m	Private Banking US$m	Other US$m	Inter-segment elimination[9] US$m	Total US$m
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 net interest income	32	17	83	1	(1)		132
Net interest income on trading activities	6	1	13			133	153
Net trading income/(expense)[7]	38	18	96	1	(1)	133	285
Net income from financial instruments designated at fair value	153		4				157
Gains less losses from financial 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
Total operating income	3,474	966	495	29	11	(13)	4,962
Net insurance claims[8]	(626)	(17)	(33)				(676)
Net operating income[4]	2,848	949	462	29	11	(13)	4,286
Loan impairment (charges)/recoveries and other credit risk provisions	(701)	(74)	2		(2)		(775)
Net operating income	2,147	875	464	29	9	(13)	3,511
Total operating expenses	(1,764)	(523)	(211)	(19)	(12)	13	(2,516)
Operating profit/(loss)	383	352	253	10	(3)		995
Share of profit in associates and joint ventures	5						5
Profit/(loss) before tax	388	352	253	10	(3)		1,000
	%	%	%	%	%		%
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[6]

	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)[12]			10,625				
Trading assets[12,13]			9,541				

Financial instruments designated at fair value[12]	199
Financial investments[12]	9,163
Deposits by banks[12]	2,862
Trading liabilities[12,13]	6,609

For footnotes, see page 89

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Interim Management Report: Business Review (continued)

Analysis by customer group and global business *(continued)*

Profit/(loss) before tax

	Half-year to 31 December 2007						
Latin America	Personal Financial Services US$m	Commercial Banking US$m	Global Banking and Markets US$m	Private Banking US$m	Other US$m	Inter-segment elimination[9] US$m	Total US$m
Net interest income	2,162	751	229	12	2	(114)	3,042
Net fee income	736	251	141	24	3		1,155
Trading income excluding net interest income	35	22	81	1	1		140
Net interest income on trading activities	4		5			114	123
Net trading income[7]	39	22	86	1	1	114	263
Net income from financial instruments designated at fair value	161		2				163
Gains less losses from financial investments	90	38	27	1	(1)		155
Gains arising from dilution of interests in associates					11		11
Dividend income	1	1	1				3
Net earned insurance premiums	790	34	39				863
Other operating income	11	57	23	4	4	(24)	75
Total operating income	3,990	1,154	548	42	20	(24)	5,730
Net insurance claims[8]	(704)	(20)	(27)				(751)
Net operating income[4]	3,286	1,134	521	42	20	(24)	4,979
Loan impairment (charges)/recoveries and other credit risk provisions	(791)	(138)	11		(4)		(922)
Net operating income	2,495	996	532	42	16	(24)	4,057
Total operating expenses	(1,994)	(609)	(270)	(27)	(10)	24	(2,886)
Operating profit	501	387	262	15	6		1,171
Share of profit in associates and joint ventures	4	1	2				7
Profit before tax	505	388	264	15	6		1,178
	%	%	%	%	%		%

Share of HSBC s profit before tax	5.0	3.9	2.6	0.1	0.1	11.7
Cost efficiency ratio	60.7	53.7	51.8	64.3	50.0	58.0

Balance sheet data[6]

	US$m	US$m	US$m	US$m	US$m	US$m
Loans and advances to customers (net)	21,680	16,243	9,935	65		47,923
Total assets	34,829	20,928	43,012	260	27	99,056
Customer accounts	30,628	15,524	13,950	1,190		61,292
Loans and advances to banks (net)[12]			10,339			
Trading assets[12,13]			10,384			
Financial instruments designated at fair value[12]			225			
Financial investments[12]			10,155			
Deposits by banks[12]			2,830			
Trading liabilities[12,13]			6,984			

For footnotes, see page 89.

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Footnotes to the Business Review

The footnotes below refer to the reconciliations of reported and underlying profit before tax, and the analyses of customer groups and global businesses on pages 13 to 27 and the geographical regions on pages 28 to 89.

1 *Columns headed Acquisitions and, in 2007, Disposals and dilution gains , comprise the net increment or decrement in profits in the current half-year (compared with the previous half-years) which are attributable to acquisitions or disposals of subsidiaries made, or dilution gains, in the relevant periods. Acquisitions and disposals are determined based on the review and analysis of the events in each period.*

2 *Currency translation is the effect of translating the results of subsidiaries and associates for the previous half-years at the average rates of exchange applicable in the current half-year.*

3 *Other income in this context comprises net trading income (see 7 below), net income from financial instruments designated at fair value, gains less losses from financial investments, gains arising from dilution of interests in associates, dividend income, net earned insurance premiums and other operating income less net insurance claims incurred and investment in liabilities to policyholders.*

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

5 *The main items reported under Other are certain property activities, unallocated investment activities including hsbc.com, centrally held investment companies, gains arising from the dilution of interests in associates, movements in the fair value of own debt designated at fair value (the rest of the Group s debt is included in Global Banking and Markets), and HSBC s holding company and financing operations. The results also include net interest earned on free capital held centrally, operating costs incurred by the head office operations in providing stewardship and central management services to HSBC, and costs incurred by the Group Service Centres and Shared Service Organisations and associated recoveries. At 30 June 2008, gains arising from the dilution of interests in associates were nil (first half of 2007: US$1.076 million; second half of 2007: US$16 million) and fair value gains on HSBC s debt designated at fair value were US$749 million (first half of 2007: US$84 million; second half of 2007: US$2,909 million).*

6 *Third party only.*

7 *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.*

8 *Net insurance claims incurred and movement in liabilities to policyholders.*

9 *Inter-segment elimination comprises (i) the costs of shared services and Group Service Centres included within Other which are recovered from customer groups, and (ii) the intra-segment funding costs of trading activities undertaken within Global Banking and Markets. HSBC s balance sheet management business reported within Global Banking and Markets, provides funding to the trading businesses. To report Global Banking and Markets net trading income on a fully funded basis, net interest income and net interest income/(expense) on trading activities are grossed up to reflect internal funding transactions prior to their elimination in the inter- segment column.*

10 *Equities includes a total gain of US$107 million in the first half of 2007 from the disposal of HSBC s investments in Euronext N.V. and the Montreal Exchange.*

11 *Other in Global Banking and Markets includes net interest earned on free capital held in the global business not assigned to products.*

12 *Assets and liabilities which were significant to Global Banking and Markets.*

13 *Trading assets and trading liabilities include derivatives.*

14 *Global Banking and Markets in Europe includes venture capital gains of US$187 million in the first half of 2008 (US$548 million in the first half of 2007: US$443 million in the second half of 2007).*

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

16 *Trading assets, financial instruments designated at fair value and financial investments held in Europe, and by Global Banking and Markets in North America, include financial assets which may be repledged or resold by counterparties.*

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H S B C H O L D I N G S P L C

Interim Management Report: Financial Review

Income statement

	Half-year to		
	30 June 2008 US$m	30 June 2007 US$m	31 December 2007 US$m
Interest income	**47,164**	43,567	48,792
Interest expense	**(25,986)**	(25,337)	(29,227)
Net interest income	**21,178**	18,230	19,565
Fee income	**13,381**	12,488	13,849
Fee expense	**(2,390)**	(1,993)	(2,342)
Net fee income	**10,991**	10,495	11,507
Trading income excluding net interest income	**639**	3,351	1,107
Net interest income on trading activities	**3,195**	2,160	3,216
Net trading income	**3,834**	5,511	4,323
Net income/(expense) from financial instruments designated at fair value	**(584)**	874	3,209
Gains less losses from financial investments	**817**	999	957
Gains arising from dilution of interests in associates		1,076	16
Dividend income	**88**	252	72
Net earned insurance premiums	**5,153**	3,977	5,099
Other operating income	**1,435**	678	761
Total operating income	**42,912**	42,092	45,509
Net insurance claims incurred and movement in liabilities to policyholders	**(3,437)**	(3,599)	(5,009)
Net operating income before loan impairment charges and other credit risk provisions	**39,475**	38,493	40,500
Loan impairment charges and other credit risk provisions	**(10,058)**	(6,346)	(10,896)
Net operating income	**29,417**	32,147	29,604
Employee compensation and benefits	**(10,925)**	(10,430)	(10,904)
General and administrative expenses	**(7,479)**	(7,022)	(8,272)
Depreciation of property, plant and equipment	**(863)**	(817)	(897)
Amortisation and impairment of intangible assets	**(346)**	(342)	(358)
Goodwill impairment	**(527)**		
Total operating expenses	**(20,140)**	(18,611)	(20,431)
Operating profit	**9,277**	13,536	9,173

Share of profit in associates and joint ventures	**970**	623	880
Profit before tax	**10,247**	14,159	10,053
Tax expense	**(1,941)**	(2,645)	(1,112)
Profit for the period	**8,306**	11,514	8,941
Profit attributable to shareholders of the parent company	**7,722**	10,895	8,238
Profit attributable to minority interests	**584**	619	703

In the first half of 2008, a period marked by significant declines in profitability throughout much of the banking industry in the most difficult financial markets for decades, HSBC produced a pre-tax profit of US$10.2 billion which, although 28 per cent lower than in the first half of 2007, demonstrated the strength and resilience of the Group s diversified business model in troubled times. On an underlying basis pre-tax profit was 25 per cent lower.

Results in the first half of 2007 benefited from US$1.1 billion of one-off dilution gains arising on shares issued by the Group s mainland China

associates: Industrial Bank, Ping An Insurance and Bank of Communications. This translated into a benefit to earnings per share of US$0.09. In the first half of 2008, results incorporated a non-cash pre- and post-tax impairment charge of US$527 million in North America Personal Financial Services. This represented US$0.04 per share.

During this period, HSBC remained profitable in all customer groups, most notably considering the market turmoil, Global Banking and Markets. In Commercial Banking and Private Banking, profits reached new heights for a six-month period, as they

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did in the developing markets operations of both Personal Financial Services and Global Banking and Markets. The Group also remained profitable in all geographical regions with the continuing exception of North America, where the consumer finance business remained heavily affected by the deepening housing market weakness and general economic slowdown. In addition, Global Banking and Markets suffered further credit turmoil-related write-downs on trading exposures and leveraged loans.

These continuing areas of weakness contrasted with the very strong financial performance across most developing markets businesses, which was augmented by significant improvements in profitability in the European businesses, which achieved good revenue growth without substantially adding to costs.

Changes in the composition of the Group in this period were modest with the only major transaction being the acquisition of the assets, liabilities and operations of The Chinese Bank in Taiwan, which was completed in March. The sale of the regional bank network in France to Banque Populaire announced in February was completed on 2 July 2008 and a gain of US$2.1 billion will be recorded in second half results.

Earnings per share declined by 32 per cent to US$0.65, with return on shareholders equity below 15 per cent. HSBC s capital ratios remained strong, with a tier one capital ratio of 8.8 per cent on a Basel II basis.

Revenues increased by US$982 million, or 3 per cent, affected significantly by the drag from the deterioration in credit quality in the US consumer finance business and write-downs in Global Banking and Markets of US$3.9 billion. Cost growth of US$1.5 billion, or 8 per cent, was slower than that reported in the first half of 2007, and primarily reflected action taken to remove costs from the underperforming US businesses. The Group s retail deposit and lending businesses, both personal and commercial, contributed strongly to revenue growth, delivering increases in net interest income and fee income of 9 per cent and 5 per cent, respectively, despite margin pressure on certain deposit products due to sharp declines in interest rates in the US and Hong Kong.

Within Global Banking and Markets emerging markets businesses, in addition to the strong revenue growth in foreign exchange and transaction banking, Balance Sheet Management recovered strongly.

Geographically, the share of profits from Hong Kong, the Rest of Asia-Pacific region and Latin America grew to 78 per cent of total Group profits.

In **Europe**, profit before tax rose by 28 per cent, with strong performances in Commercial Banking, Personal Financial Services and Private Banking. These offset credit-related write-downs which held back Global Banking and Markets, despite the good performance of Balance Sheet Management, foreign exchange and the Rates business. Operating expenses benefited from the suspension of ex gratia payments for UK overdraft fees pending legal proceedings. Gains were recorded on the sale of MasterCard shares and the disposal of the UK merchant acquiring business, and from fair value gains on certain portions of the Group s own debt. Despite deterioration in the outlook for the UK economy, credit conditions remained stable with loan impairment charges declining, partly offset by a rise in Turkey.

Pre-tax profits from HSBC s operations in **Hong Kong** of US$3.1 billion were, however, lower than the US$3.3 billion reported in the first half of 2007, a decrease of 8 per cent due to the impairment of certain of HSBC s strategic investments in the Asian region as stock markets declined. In the opinion of HSBC management, these stakes continue to deliver the market access envisaged when they were acquired.

Pre-tax profits grew in Commercial Banking and Personal Financial Services despite the adverse effects of lower interest rates on deposit spreads, driven by strong balance sheet growth through customer acquisition and new product offerings. Strong performance in Global Banking and Markets was driven by increased income from Balance Sheet Management, as falling interest rates led to a lower cost of funds and a steeper yield curve, partially offset by write-downs on exposure to monoline insurers. In Private Banking, pre-tax profits fell, largely due to a decline in the value of equities on the Hong Kong stock market compared with the first half of 2007.

Operations in the **Rest of Asia-Pacific** region reported a pre-tax profit of US$3.6 billion compared with US$3.3 billion in the first half of 2007, an increase of 8 per cent. In the first half of 2007, HSBC recognised non-recurring gains of US$1.1 billion following share offerings made by HSBC associates Ping An Insurance, Bank of Communications and Industrial Bank. Excluding these dilution gains, profit before tax increased by 49 per cent on an underlying basis.

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Interim Management Report: Financial Review (continued)

In **North America**, profitability declined by US$5.3 billion to reflect a pre-tax loss of US$2.9 billion, due to a rise in loan impairment charges in Personal Financial Services and credit-related write-downs in Global Banking and Markets which exceeded the savings in operating costs instigated by management. The ongoing restriction in credit availability in the US economy resulted in an acceleration in house price declines as refinancing opportunities remained limited. Unemployment increased and personal bankruptcies rose, resulting in a widening of the credit quality deterioration that, in 2007, had been concentrated in sub-prime mortgage portfolios. Where foreclosures could not be avoided, losses rose due to the decline in property values. The Commercial Banking business was also affected by spread compression on its deposit-taking business, and a rise in loan impairments due to provisioning for the weaker economic outlook.

In **Latin America**, pre-tax profits rose by 27 per cent, driven by Commercial Banking, where HSBC continued to use its international banking connections to expand trade finance and cross-border referrals, and Global Banking and Markets, which

benefited from strong growth in foreign exchange and Balance Sheet Management revenues. Personal Financial Services profit before tax increased on balance sheet expansion and from a number of one-off gains, partly offset by rising loan impairment charges on credit cards in Mexico as the portfolio matured.

Outside Asia, insurance operations, whose results are reported mainly in Personal Financial Services and Commercial Banking, continued to increase their contribution to the Group s results. In Asia, impairments booked against certain investments and declines in insurance assets due to weaker equity markets exceeded the contribution from associates.

HSBC s strategy of using investment stakes where appropriate to increase exposure in fast growing markets, particularly mainland China, made a material contribution to Group s results as the share of profit in associates increased by 56 per cent to US$970 million.

Net interest income

	Half-year to					
	30 June 2008		30 June 2007		31 December 2007	
	US$m	**%**	US$m	%	US$m	%
By geographical region						
Europe	**4,475**	**21.1**	3,920	21.5	3,826	19.6
Hong Kong	**2,835**	**13.4**	2,568	14.1	2,915	14.9
Rest of Asia-Pacific	**2,633**	**12.4**	1,901	10.4	2,242	11.5
North America	**7,873**	**37.2**	7,307	40.1	7,540	38.5
Latin America	**3,362**	**15.9**	2,534	13.9	3,042	15.5
Net interest income	**21,178**	**100.0**	18,230	100.0	19,565	100.0

Half-year to

	30 June 2008	30 June 2007	31 December 2007
	US$m	US$m	US$m
Net interest income	**21,178**	18,230	19,565
Average interest-earning assets	**1,420,288**	1,230,903	1,361,428
	%	%	%
Gross interest yield[1]	**6.68**	7.14	7.11
Net interest spread[2]	**3.03**	2.93	2.80
Net interest margin[3]	**3.00**	2.99	2.85

1 *Gross interest yield is the average annualised interest rate earned on average interest-earning assets (AIEA).*
2 *Net interest spread is the difference between the average annualised interest rate earned on AIEA, net of amortised premiums and loan fees, and the average annualised interest rate payable on average interest-bearing funds.*
3 *Net interest margin is net interest income expressed as an annualised percentage of AIEA.*

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Net interest income of US$21.2 billion was 16 per cent higher than in the first half of 2007, 12 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:

- turmoil in global credit markets and significant corrections to equity markets since August 2007 drove companies and individuals to shield their assets from the worst effects of the disruption. Consequently HSBC, with its strong capital base, succeeded in attracting US$17 billion of deposits in the period;
- lower average interest rates across many of the major economies of the world, as central banks cut base rates to mitigate the effects of the US house market correction and the related credit crisis;
- as interest rates fell, yield curves steepened and this, together with an increase in surplus funds following the rise in deposits noted above, led to higher Balance Sheet Management revenues;
- an expansion in the Group s trading activities led to a higher cost of funding this business. Net interest income includes the cost of funding trading assets, while the related external revenues are reported in trading income; and
- growth in commercial lending, in particular, to the mid-market segment with strongest growth in the Asia-Pacific region and in Latin America.

In **Europe**, net interest income increased by 7 per cent to US$4.5 billion, notwithstanding a 28 per cent rise in the funding costs of trading activities. In Global Banking and Markets, recent interest rate reductions in the US and Europe lowered funding costs which, together with a steeper yield curve, underpinned a tripling of Balance Sheet Management revenues. Payments and cash management net interest income increased by 8 per cent as customers sought a safe haven for their sterling funds. In Switzerland, net interest income in Private Banking rose strongly as clients switched funds from investment products to deposits as equity markets weakened. Net interest income in both Personal Financial Services and Commercial Banking was broadly in line with the first half of 2007. However, branch expansion and the resulting customer acquisition in Turkey drove higher average lending and deposit balances and increased net interest income.

Net interest income in **Hong Kong** of US$2.8 billion was 10 per cent higher than in

the first half of 2007. Higher Balance Sheet Management revenues were the primary driver of a rise in net interest income in Global Banking and Markets. Significant and deep cuts to interest rates in the US, which were followed in Hong Kong, resulted in lower funding costs and a steeper yield curve, providing increased opportunities to deploy a larger surplus pool of funds from higher deposits in the retail businesses. Net interest income in Global Banking and Markets was further boosted by a widening of lending spreads as the business took advantage of a more conservative lending environment to increase spreads.

In Personal Financial Services, a focus on Premier and the increasing attractiveness of deposits over equity investments helped to drive a rise in savings balances and a 6 per cent increase in net interest income. In Commercial Banking, net interest income rose by 6 per cent due to higher liability balances following several targeted marketing campaigns, partly offset by lower deposit spreads in the declining rate environment.

Net interest income was 32 per cent higher in **Rest of Asia-Pacific**. Lower funding costs in Global Banking and Markets drove a significant increase in Balance Sheet Management revenues for the reasons noted above. Strong economic growth stimulated a strong increase in lending balances in the Middle East, generating higher net interest income. In Personal Financial Services, growth in cards and personal lending, together with higher spreads on these asset products following lower cost of funds, generated increased revenue. In Commercial Banking, a rise in deposit volumes was the primary cause of higher net interest income as HSBC continued to focus on organic growth in the region.

In **North America**, net interest income rose by 7 per cent. This was largely due to a rebound in Balance Sheet Management.

In Personal Financial Services, net interest income was broadly in line with the first half of 2007, as the effect of lower balances as HSBC reduced the size of the consumer lending business, curtailed marketing and the ongoing running down of the mortgage services portfolio was offset by increased spreads as the cost of funds fell in the declining rate environment. In Commercial Banking, net interest income was also broadly unchanged as higher loan and deposit volumes driven by organic growth was offset by tighter deposit spreads as base rates declined.

Net interest income in **Latin America** of US$3.4 billion was 19 per cent higher than in

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the first half of 2007, largely driven by organic lending and deposit growth throughout the region, particularly in Personal Financial Services where net interest income rose by 17 per cent.

Growth in average Personal Financial Services asset balances in the region was driven by credit card sales in Mexico, albeit at a slower rate than in recent years, and by strong demand for credit in Brazil s buoyant economy. Deposit balances were boosted by competitive pricing in Mexico. The benefit of balance sheet growth was augmented by improved asset spreads. In Global Banking and Markets, higher net interest income was driven by balance

sheet management in Mexico. Net interest income in Commercial Banking rose by 10 per cent to US$800 million, largely due to increased lending volumes in Mexico, particularly in the real estate sector, and in Brazil from sales and pricing initiatives.

Average interest-earning assets of US$1,420 billion were US$189 billion higher than in the first half of 2007, while HSBC s net interest margin was broadly unchanged. Net free funds declined as a higher proportion of assets were deployed to trading activities.

Net fee income

	Half-year to					
	30 June 2008		30 June 2007		31 December 2007	
	US$m	**%**	US$m	%	US$m	%
By geographical region						
Europe	**4,223**	**38.4**	4,144	39.5	4,287	37.3
Hong Kong	**1,469**	**13.4**	1,439	13.7	1,923	16.7
Rest of Asia-Pacific	**1,338**	**12.1**	1,010	9.6	1,236	10.7
North America	**2,822**	**25.7**	2,904	27.7	2,906	25.3
Latin America	**1,139**	**10.4**	998	9.5	1,155	10.0
Net fee income	**10,991**	**100.0**	10,495	100.0	11,507	100.0

	Half-year to		
	30 June 2008	30 June 2007	31 December 2007
	US$m	US$m	US$m
Cards	**3,089**	3,092	3,404
Account services	**2,260**	1,961	2,398

Funds under management	**1,572**	1,390	1,585
Broking income	**954**	928	1,084
Insurance	**942**	804	1,032
Global custody	**757**	557	847
Credit facilities	**639**	672	466
Imports/exports	**496**	407	459
Unit trusts	**337**	420	455
Remittances	**307**	273	283
Corporate finance	**232**	220	189
Underwriting	**204**	196	171
Trust income	**164**	146	153
Taxpayer financial services	**154**	234	18
Maintenance income on operating leases	**70**	69	70
Mortgage servicing	**56**	53	56
Other	**1,148**	1,066	1,179
Total fee income	**13,381**	12,488	13,849
Less: fee expense	**(2,390)**	(1,993)	(2,342)
Net fee income	**10,991**	10,495	11,507

Net fee income increased by 5 per cent to US$11.0 billion, 1 per cent on an underlying basis. The commentary that follows is on an underlying basis.

- Card fee income decreased overall due to a substantial fall in income in the consumer finance business in the US. This decline resulted from changes in fee billing arrangements implemented in the latter part of 2007 and early 2008 to improve the customer proposition. Measures included the curtailment of the over-limit fee and enhanced billing practices. The

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decrease more than offset increased income in other countries, mainly in Mexico and the UK.

- Although the buoyant stock market performance in Hong Kong peaked in October 2007, trading volumes in the first half of 2008 were still higher than those recorded in the comparative period in 2007. Customer appetite for investment services in Asia and the Middle East drove higher income from broking services, securities services and funds under management. Despite stock market volatility, the sale of investment products rose as customers increasingly chose structured products.

In **Europe**, net fee income decreased by 4 per cent. In France, fee income decreased as the regional banks were reclassified as held for sale and their income was recorded in other operating income. Fees payable increased in the UK on brokerage, stock borrowing and lending and on cards, driven by increased transaction volumes. Card-generated income increased, mainly in the UK and Turkey, on higher transaction volumes and portfolio growth. Interchange and acquiring income increased on higher transaction volumes in the UK, while a significant rise in cash advance turnover in Turkey also resulted in higher income. The benefits offered as part of the Plus account in the UK resulted in a migration from non-fee paying current accounts to the Plus account, contributing to higher income from account services.

In **Hong Kong**, fee income rose by 2 per cent, mainly driven by business growth in the region. The number of cards in circulation grew over the comparable period in 2007 as the Group maintained its leadership position in Hong Kong and continued to be innovative in this category with the launch of the Green Credit Card. Stock market activity during the current period was higher than in the first half of 2007, resulting in increased income from broking services, securities services and funds under management. HSBC actively marketed its investment products through targeted programmes and incentives and introduced a portfolio wealth

management sales tool in the second half of 2007. In the insurance business, sales of the Life Invest protection plan increased significantly. Higher account services fee income was generated on bundled products, mainly on PowerVantage. Unit trust income decreased due to less favourable US equity market conditions.

In **Rest of Asia-Pacific**, fee income increased by 26 per cent. Cards fee income rose strongly across the region driven by growth in the number of cards in circulation, balances and card usage. Income from funds under management increased, particularly in Singapore and Japan. Increased economic activity in the Middle East resulted in higher income. The region registered strong sales of investment products and higher fees from cards and trade-related lending fees. Income on insurance and securities services also grew.

In **North America**, fee income fell by 2 per cent. In the consumer finance business, income fell on credit cards due to changes in fee billing arrangements implemented to improve the customer proposition. Insurance fee income rose as more customers took up the debt protection enhancement service on credit cards. Underwriting income grew on a number of transactions including the Visa IPO. The previously announced decision to stop offering pre-season funding loans based on the previous year s tax return led to lower fee income in Taxpayer Financial Services.

In **Latin America**, fee income increased by 4 per cent. Card fee income rose, mainly in Mexico on a higher number of cards in force and higher collection and late payment fees, mainly due to the application of stricter guidelines and higher fees charged. Income from deposit accounts continued to rise, driven by an increase in membership fees. In Brazil, a ruling by the Central Bank removing certain fees, such as charges on early loan repayments and returned cheques and the discontinuation of commissions paid by the Brazilian social security agency for pension payment services negatively affected revenues.

Net trading income

	Half-year to					
	30 June 2008		30 June 2007		31 December 2007	
	US$m	**%**	US$m	%	US$m	%
By geographical region						
Europe	**3,649**	**95.2**	3,338	60.5	3,605	83.4
Hong Kong	**314**	**8.2**	469	8.5	773	17.9
Rest of Asia-Pacific	**1,329**	**34.7**	797	14.5	846	19.5
North America	**(1,816)**	**(47.4)**	622	11.3	(1,164)	(26.9)
Latin America	**358**	**9.3**	285	5.2	263	6.1
Net trading income[1]	**3,834**	**100.0**	5,511	100.0	4,323	100.0

	Half-year to		
	30 June 2008	30 June 2007	31 December 2007
	US$m	US$m	US$m
Trading activities	**559**	3,266	1,255
Net interest income on trading activities	**3,195**	2,160	3,216
Other trading income			
Hedge ineffectiveness:			
on cash flow hedges	**(15)**	(49)	(28)
on fair value hedges	**(20)**	21	(2)
Non-qualifying hedges	**115**	113	(118)
Net trading income[1]	**3,834**	5,511	4,323

1 *The cost of internal funding of trading assets increased by US$0.8 billion compared with 30 June 2007 (decreased by US$0.3 billion compared with 31 December 2007) and 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.*

Net trading income includes US$262 million associated with changes in the fair value of issued structured notes and other hybrid instrument liabilities derived from movements in HSBC issuance spreads.

Net trading income fell by 30 per cent to US$3.8 billion due to US$3.9 billion of write-downs on credit trading, leveraged and acquisition finance, and monoline exposures, largely in the US and the UK. More information on these write-downs and the underlying assets is available on page 113. On an underlying basis the decline was 33 per cent. The following commentary is on an underlying basis.

In the prevailing conditions, the market value of certain credit instruments, most notably sub-prime residential mortgage-backed loans and structured credit instruments, deteriorated. The credit and liquidity disruption that began in the US sub-prime market spread into other mortgage and mortgage-related products. HSBC had mitigated its risk to some extent against such declines by transacting with monoline insurers to buy protection against losses from defaults. As the market turmoil worsened, the market value of this protection initially increased significantly, reflecting the market view that it was more likely that defaults would occur. The sudden increase in the potential liabilities of the monoline insurers resulted in their credit ratings being downgraded as the scale of the liabilities incurred cast significant doubt on the ability of many monoline insurers to pay. Accordingly, a credit risk write-down was taken

against the market value of the exposure to monoline insurers. HSBC also originated certain leveraged and acquisition finance loans for the purpose of syndicating or selling down to generate a trading profit. The market value of some of these loans fell due to general credit and liquidity disruption, and the loss of value is reflected in trading results.

Other than products affected by credit markets, trading performance was strong across all regions.

Foreign exchange trading maintained its excellent performance, with record trading revenues 61 per cent higher, driven by market volatility, US dollar weakness and increased customer volumes across all regions. Growth in metals revenues were achieved on the back of record commodity prices and increased investor demand, particularly for precious metals.

Credit losses of US$3.1 billion compared with income of US$658 million in the first half of 2007, due to the write-downs noted above. This included losses from structured credit derivatives. Trading in new US mortgages and related products was discontinued in late 2007.

Rates generated record trading revenues up 104 per cent, due to favourable positioning against movements in interest rate yield curves as central

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banks responses to the credit turmoil drove short-term interest rates lower. Rates revenues were also boosted by new deals and the widening of spreads, due to increased customer demand.

Excluding the effect of the gain on the sale of HSBC s investments in Euronext N.V. and the Montreal Exchange in the first half of 2007, equities trading income doubled due to increased commission and equity financing revenues.

Net trading income in **Europe** rose by 5 per cent, despite US$1.4 billion of write-downs in the UK, as discussed above. The effect of the write-downs in the UK was offset by increased Rates revenue as short-term interest rates fell and the yield curve steepened, and by increased foreign exchange revenue as exchange rate volatility drove higher customer volumes. In France, trading income grew significantly as the Rates business saw high customer demand for inflation protection products.

In **Hong Kong**, a net trading income decline of 33 per cent was caused by write-downs on exposures to monoline insurers, partly offset by higher foreign exchange revenues and significantly increased sales

of equity-linked investment products to retail customers.

Strong growth in **Rest of Asia-Pacific** came from foreign exchange and Rates trading, reflecting increased customer volumes and favourable positioning against market movements. Significant contributions to revenue growth were made in South Korea, Middle East, mainland China and India, in particular.

A net trading loss of US$1.8 billion in **North America** was due to the US$2.3 billion of write-downs in the US from the factors noted above. Other product areas performed well, notably foreign exchange and Rates. Foreign exchange benefited from the volatility in the US dollar exchange rate against most currencies, and Rates benefited from positioning correctly for the Federal Reserve s sudden and deep cuts to US interest rates, and the consequent steepening of the yield curve.

Net trading income grew by 12 per cent in **Latin America**, primarily in Brazil and Mexico, as customer demand drove higher foreign exchange volumes.

Net income/(expense) from financial instruments designated at fair value

	Half-year to 30 June 2008		**At 30 June 2008**	
	Net income/(expense) US$m	**%**	**Assets US$m**	**Liabilities US$m**
By geographical region				
Europe	**(659)**	**112.8**	**28,283**	**50,366**
Hong Kong	**(361)**	**61.8**	**7,075**	**4,218**
Rest of Asia-Pacific	**(88)**	**15.1**	**849**	**349**
North America	**368**	**(63.0)**		**34,825**
Latin America	**156**	**(26.7)**	**4,579**	
	(584)	**100.0**	**40,786**	**89,758**

	Half-year to 30 June 2007	At 30 June 2007	
	Net income	Assets	Liabilities

	US$m	%	US$m	US$m
By geographical region				
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	81	9.3		34,344
Latin America	157	18.0	2,570	
	874	100.0	34,849	75,966

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Interim Management Report: Financial Review (continued)

	Half-year to 31 December 2007		At 31 December 2007	
	Net income US$m	%	Assets US$m	Liabilities US$m
By geographical region				
Europe	878	27.4	30,058	50,077
Hong Kong	466	14.5	7,253	4,412
Rest of Asia-Pacific	33	1.0	886	501
North America	1,669	52.0		34,949
Latin America	163	5.1	3,367	
	3,209	100.0	41,564	89,939

	Half-year to		
	30 June 2008 US$m	30 June 2007 US$m	31 December 2007 US$m
Net income/(expense) arising from:			
financial assets held to meet liabilities under insurance and investment contracts	**(2,023)**	1,348	708
liabilities to customers under investment contracts	**745**	(620)	(320)
HSBC s long-term debt issued and related derivatives	**577**	284	2,528
change in own credit spread on long-term debt	**824**	172	2,883
other changes in fair value[1]	**(247)**	112	(355)
other instruments designated at fair value and related derivatives	**117**	(138)	293
Net income/(expense) from financial instruments designated at fair value	**(584)**	874	3,209

1 *Includes gains and losses arising from changes in the fair value of derivatives that are managed in conjunction with HSBC s long-term debt issued.*

HSBC may designate financial instruments at fair value in order to remove or reduce accounting mismatches in measurement or recognition, or where financial instruments are managed and their performance is evaluated together on a fair value basis. All income and expense on financial instruments for which the fair value option was taken were included in this line except for issued debt securities and related derivatives, where the interest components were shown in interest expense.

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 using interest rate swaps as part of a documented interest rate management strategy. Approximately US$67.0 billion (31 December 2007: US$66.2 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 debt. As credit spreads widen, accounting gains are booked, and the reverse is true in the event of spreads narrowing. 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. In addition, the economic relationship between the swap and own debt can be affected by relative movements in market factors, such as bond and swap rates at inception. 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 and certain liabilities under investment contracts with discretionary participation features (DPF) approximately US$16.3 billion (31 December 2007: US$16.7 billion); and

- for financial assets held by insurance operations and managed at fair value to meet liabilities under unit-linked and other investment contracts, approximately US$13.3 billion of assets (31 December 2007: US$14.0 billion).

Net income from financial assets designated at fair value which are held to support liabilities for both insurance and investment contracts, is presented as Net income from financial instruments designated at fair value . For liabilities under unit-linked and other investment contracts designated at fair value,

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changes are taken to the same income statement line to match the net income on the related assets. There is, however, a mismatch in presentation for insurance contracts and investment contracts with DPF, where the change in the value of the insurance contract liabilities is included within Net insurance claims incurred and movement in liabilities to policyholders , whereas any related asset returns are included within Net income from financial instruments designated at fair value .

A negative movement in the fair value of financial instruments designated at fair value of US$584 million compared with a positive movement of US$874 million in the first half of 2007.

Net income from financial instruments designated at fair value relating to the change in credit spread on certain long-term debt issued by HSBC Holdings and its subsidiaries increased significantly compared with the first half of 2007. Credit spreads widened significantly during the first quarter of 2008, leading to substantial positive fair value movements. However, this effect was partly reversed in the second quarter as credit spreads narrowed, leading to an overall gain of US$824 million compared with US$172 million in the first half of 2007. Over the life of this debt, these

fair value movements will fully reverse. The cumulative fair value adjustment since this policy was first applied is US$2.4 billion.

A negative movement in the fair value of assets held to meet insurance and investment contracts of US$2.0 billion compared with a positive movement US$1.3 billion in the first half of 2007. The negative movement was mainly driven by declining equity market performance in Hong Kong, France and the UK compared with strong performance in the first half of 2007, which affected the value of investments held in equity portfolios within the insurance operations. To the extent that these assets are utilised to meet liabilities held under insurance and investment contracts with DPF, the above movement is wholly or partially offset by a corresponding reduction in Net insurance claims and movement in liabilities to policyholders .

The reduction in the fair value of liabilities held under investment contracts of US$745 million compared with an increase of US$620 million in the first half of 2007, as the fall in the value of assets backing unit-linked investment contracts noted above led to a corresponding reduction in the liability to customers.

Gains less losses from financial investments

	Half-year to					
	30 June 2008		30 June 2007		31 December 2007	
	US$m	**%**	US$m	%	US$m	%
By geographical region						
Europe	**608**	**74.4**	790	79.1	536	56.0
Hong Kong	**(98)**	**(12.0)**	32	3.2	62	6.5
Rest of Asia-Pacific	**33**	**4.0**	26	2.6	12	1.3
North America	**106**	**13.0**	53	5.3	192	20.0
Latin America	**168**	**20.6**	98	9.8	155	16.2
Gains less losses from financial investments	**817**	**100.0**	999	100.0	957	100.0

Half-year to		
30 June 2008	30 June 2007	31 December 2007
US$m	US$m	US$m

Net gains from disposal of:			
debt securities	**38**	133	(13)
equity securities	**1,107**	852	1,009
other financial investments	**(11)**	14	
Impairment of equity securities	**(317)**		(39)
Gains less losses from financial investments	**817**	999	957

HSBC reported net gains of US$817 million during the first half of 2008 from the sale of financial investments, 18 per cent lower than in the first half of 2007 and 23 per cent lower on an underlying basis.

The following commentary is on an underlying basis.

In the first half of 2008, US$332 million of gains were attributable to the redemption of Visa shares following its IPO. These gains were regionally dispersed across Hong Kong, North America, Latin America and the Rest of Asia-Pacific regions as shares in Visa were allocated in the IPO to member banks and subsequently redeemed. Similarly, gains were realised on the sale of MasterCard shares, following its IPO.

In **Europe**, gains of US$608 million were 27 per cent less than in the first half of 2007. Profit on the disposal of MasterCard shares was more than offset by lower gains from the sale of equity holdings in the UK and France. In Private Banking, a gain of US$73 million was derived from the sale of HSBC s residual holding in the Hermitage Fund, which compared with US$23 million in the first half of 2007.

In **Hong Kong**, a loss of US$98 million in the first half of 2008 compared with a gain of US$32 million in the first half of 2007. The redemption of MasterCard shares, along with the gains from Visa referred to above, were more

than offset by impairments booked against certain of HSBC s strategic investments in the region. These investments were made as part of the strategic positioning of HSBC s businesses in Asia, and the write-downs were required following significant falls in equity market prices.

In **North America**, gains of US$106 million were 89 per cent higher than in the first half of 2007, largely due to the Visa share redemption. This increase was marginally offset by lower gains from the sale of debt securities due to less favourable market conditions compared with the first half of 2007.

Gains of US$168 million in **Latin America** were 50 per cent higher than in the first half of 2007, principally due to Visa gains in Mexico, Central America and Brazil. In the latter, gains were lower than in the first half of 2007, which included the gain on sale of an equity holding related to a credit bureau.

Net earned insurance premiums

	Half-year to					
	30 June 2008		30 June 2007		31 December 2007	
	US$m	**%**	US$m	%	US$m	%
By geographical region						
Europe	**2,286**	**44.4**	1,480	37.2	2,530	49.6
Hong Kong	**1,650**	**32.0**	1,426	35.9	1,371	26.9
Rest of Asia-Pacific	**114**	**2.2**	109	2.7	117	2.3
North America	**203**	**3.9**	231	5.8	218	4.3
Latin America	**900**	**17.5**	731	18.4	863	16.9
Net earned insurance premiums	**5,153**	**100.0**	3,977	100.0	5,099	100.0

	Half-year to		
	30 June	30 June	31 December

	2007	2007	2007
	US$m	US$m	US$m
Gross insurance premium income	**6,591**	4,532	6,469
Reinsurance premiums	**(1,438)**	(555)	(1,370)
Net earned insurance premiums	**5,153**	3,977	5,099

Net earned insurance premiums increased by 30 per cent to US$5.2 billion. HSBC acquired the remaining 51 per cent interest in HSBC Assurances in France in March 2007 and sold the Hamilton Insurance Company Limited and Hamilton Life Assurance Company Limited in the UK in October 2007. On an underlying basis, net earned insurance premiums increased by 11 per cent.

The commentary that follows is on an underlying basis.

In **Europe**, net earned insurance premiums increased by 10 per cent, primarily driven by the UK business, which launched the new Guaranteed

Income Bond in June 2007 within the life insurance business. UK net insurance premiums were also boosted by a reclassification of certain pension contracts as insurance rather than investment products following the addition of enhanced life insurance benefits. In France, net insurance premiums in the first half of 2008 were reduced by a reinsurance transaction which passed insurance premiums to a third party reinsurance provider. Excluding this, gross premiums in France increased as a result of promotional offers during the first half of 2008.

In **Hong Kong**, net earned insurance premiums of US$1.7 billion were 15 per cent higher than in the

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first half of 2007. Higher premium income from the life insurance business was driven by increased sales of endowment savings products in Hang Seng Life, which was the leading writer of life insurance new business in Hong Kong in the first quarter of 2008, with a market share of 16 per cent. The fluctuating investment market and lower interest rate environment helped the growth of the life insurance business as customers sought more secure, steady growth products.

In the **Rest of Asia-Pacific** region, net insurance premiums were 4 per cent lower than in the first half of 2007. Increased life insurance business in Singapore, mainly due to growth of the Life Manager Plus product, which was launched in March 2007, was offset by a decline in Malaysia, due to the non-recurrence of income from a closed-end fund, sold for a one month period in the first half of 2007.

In **North America**, net insurance premiums decreased by 13 per cent. Life insurance premiums fell as credit life products in North America declined due to falling loan volumes within HSBC Finance, which led to a reduction in income from associated credit protection products. These declines were

partially offset by increased sales of a simplified issue term life product, which was launched in 2007 and rolled out across all states in the second half of the year. Non-life insurance premiums also fell, due to lower loan origination.

In **Latin America**, net earned insurance premiums rose to US$900 million, an increase of 11 per cent. This was mainly driven by an increase in Brazil in the level of voluntary pension fund contributions. The number of pension fund contracts in force in Brazil increased by 7 per cent, as a result of sales initiatives designed to attract new customers. In Mexico, growth reflected an increase in life, personal accident and vehicle products. An increased focus on life insurance sales through HSBC and other distribution channels, made a significant contribution to growth. Vehicle insurance premiums also increased in Argentina as prices rose in response to underlying vehicle price inflation. Life insurance premium income decreased in Argentina due to the cessation of part of the pension business as a consequence of a change in government legislation.

Other operating income

	Half-year to					
	30 June 2008		30 June 2007		31 December 2007	
	US$m	**%**	US$m	%	US$m	%
By geographical region						
Europe	**1,427**	**54.8**	262	17.1	931	49.2
Hong Kong	**448**	**17.2**	413	27.0	432	22.8
Rest of Asia-Pacific	**484**	**18.6**	360	23.5	438	23.1
North America	**115**	**4.4**	342	22.4	18	0.9
Latin America	**130**	**5.0**	153	10.0	75	4.0
	2,604	**100.0**	1,530	100.0	1,894	100.0
Intra-HSBC elimination	**(1,169)**		(852)		(1,133)	
Other operating income	**1,435**		678		761	

	Half-year to		
	30 June 2008	30 June 2007	31 December 2007

	US$m	US$m	US$m
Rent received	**326**	315	315
Gain/(loss) on assets held for sale	**(16)**	(37)	42
Valuation gains on investment properties	**27**	48	104
Gain on disposal of property, plant and equipment, intangible assets and non-financial investments	**412**	152	61
Change in present value of in-force long-term insurance business	**324**	(155)	10
Other	**362**	355	229
Other operating income	**1,435**	678	761

Other operating income of US$1.4 billion was US$757 million, or 112 per cent, higher than in the first half of 2007, an 84 per cent increase on an underlying basis.

The commentary that follows is on an underlying basis.

In **Europe**, other operating income increased significantly. In the UK, other operating income included a gain on the sale of a merchant acquiring business to a joint venture with Global Payments Inc. This income line also benefited from a non-recurring reduction in the PVIF in 2007 following a change in FSA regulations. In 2008, a pension product was enhanced with life insurance features and reclassified as an insurance product, resulting in an uplift to PVIF. Gain on sale and leaseback of branches increased as 140 branches were sold in the first half of 2008 compared with 12 in the comparative period in 2007. In France, the regional banks were reclassified as held for sale following a decision to sell them, resulting in their profits of US$32 million for the half-year being reported in other operating income.

In **Hong Kong**, other operating income remained broadly unchanged.

Other operating income in **Rest of Asia-Pacific** rose by 13 per cent, mostly driven by recharges from increased business volumes at the Group Service Centres.

In **North America**, other operating income decreased due to higher losses on repossessed properties driven by an increase in foreclosures and continuing falls in house prices. Further losses were incurred on the sale of investment in two funds due to adverse market conditions. A loss was registered on the sale of a brokerage business which was not considered to be part of the strategic operations of the group. Gains in the first half of 2007 were boosted by the sale and leaseback of an HSBC building.

In **Latin America**, other operating income declined due to the non-recurrence of the gain recorded in Mexico in the first half of 2007, following a refinement of the income recognition methodology in respect of long-term insurance products. This was partially offset by a similar gain of US$45 million in Brazil in the current period. Further gains were registered on expired investment contracts and on the disposal of property.

Net insurance claims incurred and movement in liabilities to policyholders

	Half-year to					
	30 June 2008		30 June 2007		31 December 2007	
	US$m	**%**	US$m	%	US$m	%
By geographical region						
Europe	**1,388**	**40.4**	1,146	31.8	2,333	46.6
Hong Kong	**1,169**	**34.0**	1,512	42.1	1,696	33.9
Rest of Asia-Pacific	**4**	**0.1**	141	3.9	112	2.2
North America	**112**	**3.3**	124	3.4	117	2.3
Latin America	**764**	**22.2**	676	18.8	751	15.0
Net insurance claims incurred and movement in liabilities to policyholders[1]	**3,437**	**100.0**	3,599	100.0	5,009	100.0

	Half-year to		
	30 June 2008	30 June 2007	31 December 2007

	US$m	US$m	US$m
Gross insurance claims and movement in liabilities to policyholders	**4,769**	3,428	6,122
Reinsurers share of claims incurred and movement in liabilities to policyholders	**(1,332)**	171	(1,113)
Net insurance claims incurred and movement in liabilities to policyholders[1]	**3,437**	3,599	5,009

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

Net insurance claims incurred and movement in liabilities to policyholders decreased by 5 per cent compared with the first half of 2007, to US$3.4 billion. HSBC acquired the remaining shares in HSBC Assurances in France in March 2007 and sold the Hamilton Insurance Company Limited and

Hamilton Life Assurance Company Limited in the UK in October 2007. Net insurance claims incurred and movement in liabilities to policyholders decreased by 14 per cent on an underlying basis.

The commentary that follows is on an underlying basis.

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In **Europe**, net insurance claims incurred and movement in liabilities to policyholders rose by 1 per cent to US$1.4 billion. This was mainly due to a release of policyholder liabilities in the UK in the first half of 2007 following revised regulatory guidance issued by the FSA and by the rise in new liabilities associated with the launch of the Guaranteed Income Bond by HSBC Life in June 2007. This was offset by a reduction in policyholder provisions in France which reflected the creation of a reinsurance asset with a third party insurer on a portion of the life insurance business. Falling values of assets within the investment portfolio flowed through to lower liabilities on associated policies.

In **Hong Kong**, reductions in net insurance claims incurred and in liabilities to policyholders of 23 per cent reflected lower stock market values in Hong Kong, which fed through to a decrease in the value of unit-linked and participating funds.

In **Rest of Asia-Pacific**, similarly, a reduction in net insurance claims incurred and movement in liabilities to policyholders of 97 per cent was due to

falling equity markets affecting unit-linked and participating life insurance products.

In **North America**, net insurance claims incurred and movement in liabilities to policyholders fell by 10 per cent. Life insurance claims fell, mostly due to a fall in credit life payments in the consumer lending business, in line with the fall in premiums. This was partly offset by an increase in provisions from the new simplified issue term life insurance product, due to an increase in sales.

In **Latin America**, net insurance claims incurred and movement in liabilities to policyholders were in line with the first half of 2007. In the life insurance business, the benefit of a higher level voluntary pension fund contributions in Brazil was largely offset by the cessation of part of the pension business in Argentina. An increase in non-life insurance claims was driven by the vehicle insurance business in Argentina, which experienced a higher frequency of vehicle related claims in line with greater sales of vehicle contracts, combined with an increase in the value of claims due to rising levels of inflation.

Loan impairment charges and other credit risk provisions

	Half-year to					
	30 June 2008		30 June 2007		31 December 2007	
	US$m	**%**	US$m	%	US$m	%
By geographical region						
Europe	**1,272**	**12.6**	1,363	21.5	1,179	10.8
Hong Kong	**81**	**0.8**	80	1.3	151	1.4
Rest of Asia-Pacific	**369**	**3.7**	308	4.8	308	2.8
North America	**7,166**	**71.3**	3,820	60.2	8,336	76.5
Latin America	**1,170**	**11.6**	775	12.2	922	8.5
Loan impairment charges and other credit risk provisions	**10,058**	**100.0**	6,346	100.0	10,896	100.0

	Half-year to		
	30 June 2008 US$m	30 June 2007 US$m	31 December 2007 US$m
Loan impairment charges			
New allowances net of allowance releases	**10,436**	6,635	11,547
Recoveries of amounts previously written off	**(479)**	(307)	(698)

	9,957	6,328	10,849
Individually assessed allowances	**332**	385	411
Collectively assessed allowances	**9,625**	5,943	10,438
Impairment of available-for-sale debt securities	**67**		44
Other credit risk provisions	**34**	18	3
Loan impairment charges and other credit risk provisions	**10,058**	6,346	10,896
Customer impaired loans	**19,029**	14,555	18,304
Customer loan impairment allowances	**20,580**	14,323	19,205

Loan impairment charges and other credit risk provisions were US$10.1 billion, a 58 per cent increase compared with the first half of 2007, 55 per cent on an underlying basis. The analysis that follows is on an underlying basis.

Loan impairment charges rose by 55 per cent, primarily due to:

- significant increases in US Personal Financial Services. Delinquency levels rose as US consumers continued to be affected by continuing falling house prices, tighter credit conditions which reduced their options for refinancing, a weakening economy with rising unemployment and higher food and fuel costs;

- sharp increases in loan impairment charges in the high growth regions of Turkey, India and Mexico as personal lending rose. This reflected higher delinquency rates as the deterioration in credit quality coincided with balances maturing in a weaker economic environment following strong organic growth.

In **Europe**, loan impairment charges fell by 7 per cent. Charges in the UK consumer finance business declined following a methodology change which resulted in a one-off increase in charges in the first half of 2007 and reduced balances. In the UK bank, loan impairment charges were broadly in line with the first half of 2007 as lower charges in Personal Financial Services, following the sale of part of the cards portfolio in October 2007, were offset by higher charges in Global Banking and Markets, which although still reflecting low levels of corporate defaults, compared with net recoveries in the first half of 2007. Impairment charges for residential mortgage loans remained low despite the progressive weakening in the housing market. In Turkey, loan impairment charges more than trebled, primarily within Personal Financial Services. Higher lending and increased delinquency rates in credit cards and personal lending drove charges higher as consumers found it more difficult to repay their existing debts in the current economic environment.

In **Hong Kong**, loan impairment charges were in line with the first half of 2007 despite modest balance growth, due to lower charges on credit cards and mortgages within Personal Financial Services. Credit quality remained sound.

In **Rest of Asia-Pacific**, loan impairment charges rose by 15 per cent, primarily due to lending growth across the Middle East and India. Charges in India rose due to volume growth in the personal loans, consumer finance, and cards portfolios, and a more challenging credit environment for personal

customers in which debt repayment was adversely affected by high inflation and interest rates. Loan impairment charges rose in the Middle East, driven by balance growth and higher delinquency rates in the UAE as HSBC broadened its offerings in the credit card market by extending into customer groups with a higher probability of default but which are attractive on a risk adjusted basis. This was partly offset by higher recoveries from commercial customers. In Asia, loan impairment charges in Taiwan fell due to the continued recovery from the 2006 credit crisis, which had previously resulted in substantial loan impairment charges following regulatory intervention in the card market. In Thailand, loan impairment charges fell as higher-risk commercial banking relationships were closed in order to reduce credit risk in the loan portfolio.

In **North America**, loan impairment charges were significantly higher than in the first half of 2007 driven by the US, where delinquency rates increased as a result of a deteriorating economy, higher unemployment, an accelerated decline in house prices and increased bankruptcy filings. Credit quality, led by sub-prime lending, declined across the portfolio, while prime and near-prime portfolios also showed some increased delinquency. In the mortgage services business, credit quality continued to deteriorate as house price falls accelerated and refinancing remained difficult. Further credit quality deterioration was also apparent in consumer lending, due to the factors discussed above. In the US retail bank, loan impairment charges rose, primarily due to a decline in credit quality within the Home Equity Line of Credit and Home Equity Loan portfolios of second lien mortgages. Although the prime residential mortgage portfolio also demonstrated some signs of increasing delinquency, credit impairment charges remained very low in dollar terms. Loan impairment charges rose most in states with higher unemployment rates and where house price appreciation had been the greatest. In the credit card business, increased loan impairment charges reflected higher levels of non-prime balances, portfolio seasoning, increased unemployment and bankruptcy filings, and the general effect of weakening in the economy. In Canada, the increase in loan impairment charges in Personal Financial Services was driven by balance growth and portfolio seasoning in the unsecured personal lending and mortgage portfolios within the consumer finance businesses. Loan impairment charges in Commercial Banking in North America more than tripled. In the US retail bank, charges rose due to worsening economic conditions, leading to customer downgrades across all business segments. In Canada, charges increased as delinquency rates rose in the

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manufacturing and export sectors as a result of the slowing US economy, higher energy costs and the weaker US dollar.

In **Latin America**, the combination of growth in unsecured lending, particularly credit cards, and higher delinquency rates in Mexico led to a 34 per cent rise in loan impairment charges. The majority of the increase arose in Mexico due to balance growth and higher delinquency rates in the credit card and personal loan portfolios as balances matured. This increase in loan impairment charges was, in part, a planned cost of building strong market share through organic growth in an area where HSBC was previously under-represented. Management actions in the second half of 2007 and in 2008, taken in response to rising delinquencies, slowed growth in card numbers significantly and also reduced sales of lending products to lower credit quality customers. In Brazil, loan impairment charges rose from the

first half of 2007, driven by deterioration in credit quality in vehicle finance and store loans, partly offset by the sale of an impaired loan portfolio in Personal Financial Services in March 2008.

The aggregate outstanding customer loan impairment allowances at 30 June 2008 of US$20.6 billion represented 2.0 per cent of gross customer advances (net of reverse repos and settlement accounts) compared with 1.6 per cent at 30 June 2007.

Impaired loans to customers were US$19.0 billion at 30 June 2008, compared with US$18.3 billion at 31 December 2007. At constant exchange rates, impaired loans increased by 26 per cent compared with 30 June 2007, while underlying lending growth (excluding lending to the financial sector and settlement accounts) was 5 per cent.

Operating expenses

	Half-year to					
	30 June 2008		30 June 2007		31 December 2007	
	US$m	**%**	US$m	%	US$m	%
By geographical region						
Europe	**8,193**	**38.4**	7,972	40.9	8,553	39.7
Hong Kong	**1,975**	**9.3**	1,665	8.6	2,115	9.8
Rest of Asia-Pacific	**2,784**	**13.1**	2,075	10.7	2,689	12.5
North America	**5,334**	**25.0**	5,235	26.9	5,321	24.7
Latin America	**3,023**	**14.2**	2,516	12.9	2,886	13.3
	21,309	**100.0**	19,463	100.0	21,564	100.0
Intra-HSBC elimination	**(1,169)**		(852)		(1,133)	
Operating expenses	**20,140**		18,611		20,431	

	Half-year to		
	30 June 2008 US$m	30 June 2007 US$m	31 December 2007 US$m
By expense category			
Employee compensation and benefits	**10,925**	10,430	10,904
Premises and equipment (excluding depreciation)	**2,137**	1,848	2,118
General and administrative expenses	**5,342**	5,174	6,154

Administrative expenses	**18,404**	17,452	19,176
Depreciation of property, plant and equipment	**863**	817	897
Amortisation and impairment of intangible assets	**346**	342	358
Goodwill impairment	**527**		
Operating expenses	**20,140**	18,611	20,431

	At 30 June 2008	At 30 June 2007	At 31 December 2007
Staff numbers (full-time equivalent)			
Europe	**84,457**	80,912	82,166
Hong Kong	**29,467**	27,066	27,655
Rest of Asia-Pacific	**93,747**	81,031	88,573
North America	**48,069**	56,693	52,722
Latin America	**63,851**	66,875	64,404
	319,591	312,577	315,520

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Interim Management Report: Financial Review (continued)

Operating expenses increased by US$1.5 billion to US$20.1 billion. On an underlying basis, cost growth was 4 per cent, the main drivers being:

- in Rest of Asia-Pacific, HSBC continued to invest in India and mainland China through increased staff numbers to support growth in business volumes. In the Middle East, staff numbers also increased, predominantly in customer facing roles. Similarly, costs rose in Hong Kong. In Europe, headcount and administrative costs in Turkey grew as the branch network was extended; and
- management s decision in the US in 2007 to close the Decision One mortgage brokerage business, cease the acquisition of mortgages from correspondent banks and brokers and reduce the consumer lending branch network in the US helped control costs. Marketing expenditure on credit card origination was curtailed to limit growth in loan balances.

In **Europe**, costs decreased by 1 per cent, compared with an increase of 6 per cent in net operating income before loan impairment charges. The main drivers of this decrease were businesses in the UK and France, partially offset by higher costs in Turkey and Switzerland. In the UK, costs declined, in part due to the non-recurrence of ex gratia payments in respect of overdraft fees applied in previous years which were expensed in 2007. A reduction in defined benefit pension costs, the result of an updated actuarial assessment, also decreased costs. Lower performance bonuses in Global Banking and Markets reflected the lower profits being earned in the current conditions. In France, reported costs decreased as the regional banks were classified as held for sale and all relevant income and costs were therefore reported in other operating income. Business expansion in Turkey was reflected in an increase of 84 branches and 220 ATMs over the first half of 2007. Staff numbers increased by 35 per cent resulting in higher staff, premises and marketing costs. Higher business transaction volumes arising from organic growth strategy and inflation, also pushed costs up. In Private Banking, costs rose, mainly due to a non-recurring saving in pension costs in 2007, and general business expansion.

In **Hong Kong**, operating expenses increased by 18 per cent, compared with growth of 1 per cent in net operating income before loan impairment charges. Inflation and business growth were the main drivers behind the increase in costs. Staff numbers increased as additional capacity was required to meet growing business needs, contributing to a 9 per cent

increase in staff costs. Rental costs increased under inflationary pressures. IT cost growth reflected business growth and the expansion of self-service banking coverage. Call centres were increasingly used to generate sales at lower costs.

Operating costs increased by 27 per cent in **Rest of Asia-Pacific** compared with a 33 per cent growth in net operating income before loan impairment charges. The main driver of cost growth remained the significant organic business expansion in the region, most notably in the Middle East, mainland China and India. Staff costs rose on increases in headcount and performance-related bonuses due to higher revenue. Growth in IT and premises and equipment costs were driven by the opening of 10 additional branches in the Middle East and 29 outlets in mainland China where Hang Seng Bank also opened 14. Marketing costs increased in the Middle East. Costs in India also rose on higher fees paid to collection agencies.

In **North America**, operating expenses increased by 2 per cent, compared with lower net operating income before loan impairment charges of 17 per cent. The increase in costs was driven by an impairment charge of US$527 million in the goodwill carried by Personal Financial Services in North America. For further information see Note 20 to the Financial Statements. Excluding this impairment charge, operating expenses declined by 8 per cent. Consumer finance continued to implement its business rationalisation programme commenced in 2007, with staff numbers decreasing due to the reduction in the number of branches, the closure of Decision One and the correspondent channel, and the transfer of certain operations and support for card and retail services to Group Service Centres. Also as part of this strategy, marketing expenditure was curtailed in an effort to restrict lending growth. In the retail bank, litigation expenses recorded in the latter part of 2007, arising from an indemnification agreement with Visa, were released following redemption of the company s shares in the IPO. In Global Banking and Markets, discretionary bonuses decreased due to lower performance in the Global Markets business. Operating expenses rose in Canada on higher staff costs driven by increased staff numbers in the retail bank and a rise in support costs. This was partly offset by lower costs in consumer finance as a result of reduced headcount following branch closures in 2007 and the sale of a mortgage brokerage business in 2008.

In **Latin America**, operating expenses grew by 8 per cent compared with growth in net operating income before loan impairment charges of 15 per

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cent. In Mexico, staff costs rose, even though headcount numbers decreased. Salary costs grew following the annual salary review at the start of the year. Costs on the Tu Cuenta cashback facility rose as usage increased. Ongoing upgrading work on the branch and ATM retail network resulted in higher property rental costs and software maintenance and development. Inflationary pressures in Argentina resulted in higher operating expenditure, particularly staff costs, following a union agreement. Cost

growth in Brazil was mitigated by a recovery of transactional taxes paid in earlier years, following a court ruling. An agreement reached with the employees unions in the second half of 2007 resulted in higher salaries and wages partially offset by lower headcount. Non-staff expenses increased with higher outsourcing costs on phone services and collections, and improvement of operational processes for debit and credit cards.

	Half-year to		
Cost efficiency ratios	**30 June 2008 %**	30 June 2007 %	31 December 2007 %
HSBC	**51.0**	48.3	50.4
Personal Financial Services	**49.5**	50.0	50.6
Europe	**57.3**	65.4	64.2
Hong Kong	**29.1**	27.6	26.9
Rest of Asia-Pacific	**68.7**	68.9	78.3
North America	**44.6**	41.8	42.8
Latin America	**57.4**	61.9	60.7
Commercial Banking	**40.2**	44.2	45.4
Europe	**39.4**	48.1	50.3
Hong Kong	**23.7**	24.5	25.4
Rest of Asia-Pacific	**40.3**	39.3	46.1
North America	**44.7**	46.4	43.8
Latin America	**55.2**	55.1	53.7

Share of profit in associates and joint ventures

	Half-year to					
	30 June 2008		30 June 2007		31 December 2007	
	US$m	**%**	US$m	%	US$m	%
By geographical region						
Europe	**1**	**0.1**	88	14.1	7	0.8
Hong Kong	**21**	**2.2**	13	2.1	15	1.7
Rest of Asia-Pacific	**936**	**96.5**	507	81.4	841	95.6
North America	**8**	**0.8**	10	1.6	10	1.1
Latin America	**4**	**0.4**	5	0.8	7	0.8
Share of profit in associates and joint ventures	**970**	**100.0**	623	100.0	880	100.0

	Half-year to		
	30 June 2008 US$m	30 June 2007 US$m	31 December 2007 US$m
Bank of Communications	**349**	190	255
Ping An Insurance	**297**	144	374
Industrial Bank	**102**	50	78
The Saudi British Bank	**146**	101	115
Other	**47**	122	37
Share of profit in:			
associates	**941**	607	859
joint ventures	**29**	16	21
Share of profit in associates and joint ventures	**970**	623	880

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Interim Management Report: Financial Review (continued)

Share of profit in associates and joint ventures was US$970 million, an increase of 56 per cent compared with the first half of 2007, and 46 per cent on an underlying basis. The commentary that follows is on an underlying basis.

Higher share of profit from associates and joint ventures was driven by Rest of Asia-Pacific, as contributions from Ping An Insurance, Bank of Communications, Industrial Bank, and The Saudi British Bank rose due to strong economic growth in the region since the first half of 2007.

- HSBC s share of profit from the Bank of Communications rose by 68 per cent, primarily due to higher net interest income driven by wider spreads as the base rate rose in mainland China, and balance sheet growth as a result of the rapid growth of the mainland China economy. Fee income rose strongly, driven by the asset custody business, financial advisory services and higher fees from bank card transactions.
- HSBC s share of profits from Ping An Insurance increased by 87 per cent following strong growth in the life insurance business, reflecting the strength of the mainland Chinese economy.
- Profits from Industrial Bank rose due to balance sheet growth, and a higher net interest margin as a result of loan repricing.
- Profits from the Saudi British Bank rose by 25 per cent due to strong balance sheet growth, particularly in the lending portfolio, as a result of the buoyant Saudi economy, and an increase in demand for project financing in the corporate sector.

Asset deployment

	At 30 June 2008		At 30 June 2007		At 31 December 2007	
	US$m	**%**	US$m	%	US$m	%
Loans and advances to customers	**1,049,200**	**41.2**	928,101	43.2	981,548	41.7
Loans and advances to banks	**256,981**	**10.1**	214,645	10.0	237,366	10.1
Trading assets	**473,537**	**18.6**	424,645	19.7	445,968	18.9
Financial investments	**274,750**	**10.8**	233,001	10.8	283,000	12.0
Derivatives	**260,664**	**10.2**	149,181	6.9	187,854	8.0
Goodwill and intangible assets	**40,814**	**1.6**	38,445	1.8	39,689	1.7
Other	**190,732**	**7.5**	162,423	7.6	178,841	7.6
	2,546,678	**100.0**	2,150,441	100.0	2,354,266	100.0
Loans and advances to customers include:						
reverse repos	**55,489**		38,023		44,898	
settlement accounts	**3,787**		3,948		2,367	

Loans and advances to banks include:			
reverse repos	**59,869**	49,990	59,141
settlement accounts	**5,083**	3,769	2,222

HSBC s total assets at 30 June 2008 were US$2,547 billion, an increase of US$192 billion or 8 per cent since 31 December 2007, mainly due to Global Banking and Markets.

At 30 June 2008, HSBC s balance sheet remained highly liquid. The proportion of assets deployed in loans and advances to customers declined to 41 per cent, while derivative assets increased to 10 per cent. Financial investments declined to 11 per cent of total assets. These changes are discussed below.

Acquisitions added US$2.1 billion to total assets. On an underlying basis, total assets grew by 7 per cent.

The commentary that follows is on an underlying basis.

Customer advances rose by 6 per cent compared with the position at 31 December 2007. There was growth in most regions, particularly Europe. In the UK, increased overdrafts with certain key customers together with growth in the reverse repo business drove higher loans and advances. This was partly offset by a decline in the US, due to the investment of a greater proportion of surplus funds in bank securities and a reduction in personal lending as a result of decisions taken to cease new originations for certain loan portfolios and tighten underwriting criteria to match risk appetite.

Loans and advances to banks increased by 6 per cent particularly in Hong Kong, Rest of Asia-Pacific and North America, as funds were increasingly invested in lower risk investments, including US treasury bills.

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Trading assets, financial investments and derivatives

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 in the balance sheet at fair value, with movements in fair value recognised in the income statement.

Trading assets of US$474 billion at 30 June 2008 were 4 per cent higher than at 31 December 2007. The increase was mainly due to the growth of the collateralised lending business in Europe, though the rate of growth slowed over the reporting period. Debt securities rose in line with the strong performance in the Rates business as a result of the higher trading activity and demand for Rates products. Holdings in equity securities fell in the first half of 2008 due to a reduction in trading positions since year end following the considerable growth in many key equity products areas in 2007.

Financial investments primarily include debt and equity instruments that are classified as held for sale or, to a lesser extent, held to maturity. The held for sale investments generally 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. In addition, financial investments include a portfolio of ABSs held by securities investment conduits (SICs) that are consolidated into the Group balance sheet. More information on these SICs and the underlying assets is available on pages 137 to 151. All financial investments are carried at fair value with unrealised gains and losses from movements thereon reported in equity until disposal. On disposal, the accumulated unrealised gain or loss is recognised through the income statement and reported as Gains less losses from financial investments .

Financial investments fell by 4 per cent compared with the reported figures at 31 December 2007. Investors in Cullinan Finance Ltd and Asscher Finance Ltd, two SIVs managed by HSBC and consolidated in 2007, were offered the opportunity to exchange their investments for notes in new SIVs, and during the first half of 2008 most of them accepted. In total, holdings in ABSs decreased due to a combination of asset sales, amortisations and write-downs. Net unrealised gains from the valuation of equities amounted to US$2.4 billion.

Derivatives are financial instruments that derive their value from the price of an underlying item. HSBC transacts derivatives for three primary purposes: to create risk management solutions for clients, for proprietary trading purposes, and to manage and mitigate HSBC s own risks.

Derivative assets of US$261 billion rose by 36 per cent from 31 December 2007, primarily across foreign exchange, interest rate and credit derivatives. The main drivers of growth were mark-to-market movement across the entire portfolio arising from volatility and movements in interest rates and credit spreads, as well as new transactions during the period. Interest rate derivatives increased in value in the UK and France, particularly in the first quarter, as customers reacted to the fall in central bank interest rates and the consequent steepening of the yield curve. Widening credit spreads in the US, caused by the general turmoil in the credit markets, led to a significant mark-to-market increase in the value of credit derivative assets and liabilities. Again, this effect was substantially seen in the first quarter. Further growth in the US and much of the growth in the UK came from foreign exchange derivatives, as continuing currency volatility and, in particular, the declining US dollar drove customer demand.

Funds under management

Funds under management at 30 June 2008 were US$857 billion, an increase of 2 per cent when compared with 31 December 2007. Both Global Asset Management and Private Banking fund holdings increased, despite both businesses being negatively affected by poor equity market performance.

Global Asset Management funds increased to US$389 billion. Net new money, driven by clients moving their funds to money market investments, and favourable foreign exchange movements were partly offset by a weaker investment performance caused by turbulent markets. Notwithstanding a decrease in emerging markets funds during the first half of 2008, Global Asset Management remains one of the world s largest emerging market asset managers, with US$86 billion of funds under management, an increase of 18 per cent since 30 June 2007.

Private Banking funds increased by 5 per cent to US$289 billion, driven primarily by foreign exchange movements and net new money of US$5 billion, offset by a poor equity market performance.

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Client assets, which provide an indicator of overall Private Banking volumes and include funds under management, were broadly unchanged at US$421 billion, with net new money of

US$15 billion offset by negative market performance. Other funds under management, of which the main element is a corporate trust business in Asia, decreased to US$174 billion.

	Half-year to		
	30 June 2008 US$bn	30 June 2007 US$bn	31 December 2007 US$bn
Funds under management			
At beginning of period	**844**	695	787
Net new money	**23**	15	21
Value change	**(49)**	36	17
Exchange and other	**39**	41	19
At end of period	**857**	787	844
Funds under management by business			
HSBC Global Asset Management	**389**	343	380
Private Banking	**289**	274	275
Affiliates	**5**	2	3
Other	**174**	168	186
	857	787	844

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 2008, assets held by HSBC as custodian amounted to US$5.1 trillion, compared with US$5.3 trillion held at 31 December 2007.

Administration includes the provision of various support function activities including the valuation of portfolios of securities and other financial assets on behalf of clients. At 30 June 2008, the value of assets held under administration by the Group amounted to US$3.5 trillion, compared with US$3.3 trillion held at 31 December 2007.

Review of transactions with related parties

As required by the FSA s Disclosure and Transparency Rules, the Board has undertaken a fair review of related party transactions that have taken place in the first six months of the current financial year; and any changes in the related party transactions described in the *Annual Report and Accounts 2007*. Pursuant to this review, where transactions and balances with related parties have a material effect on the financial position or performance of HSBC they have been disclosed in the Notes on the Financial Statements.

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 (adding back goodwill impaired) 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 ahead of 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 decreased by US$3.7 billion, or 74 per cent, compared with the first half of 2007. Profit attributable decreased, while average shareholders equity grew. The decline in profits was mainly driven by an increase of US$3.7 billion in loan impairment charges, led by the consumer finance business in the US, and by US$3.9 billion of write-downs on credit trading, leveraged and acquisition finance, and monoline exposures. The comparative period included dilution gains of US$1.1 billion which did not recur. The decrease in economic profit was also reflected in a lower return on average invested capital and, in consequence, economic spread, which decreased by 6.5 percentage points compared with the first half of 2007.

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Economic profit

	Half-year to					
	30 June 2008 US$m	**%[1]**	30 June 2007 US$m	%[1]	31 December 2007 US$m	%[1]
Average total shareholders equity	**128,409**		114,776		125,825	
Adjusted by:						
Goodwill previously amortised or written off	**8,304**		8,172		8,172	
Property revaluation reserves	**(847)**		(917)		(879)	
Reserves representing unrealised gains on effective cash flow hedges	**1,069**		215		632	
Reserves representing unrealised (gains)/losses on available-for-sale securities	**3,989**		(2,214)		(1,627)	
Preference shares and other equity instruments	**(1,939)**		(1,405)		(1,405)	
Average invested capital[2]	**138,985**		118,627		130,718	
Return on invested capital[3]	**8,204**	**11.9**	10,850	18.4	8,193	12.4
Benchmark cost of capital	**(6,911)**	**(10.0)**	(5,883)	(10.0)	(6,589)	(10.0)
Economic profit/spread	**1,293**	**1.9**	4,967	8.4	1,604	2.4

1 *Expressed as a percentage of average invested capital.*

2 *Average invested capital is measured as average total shareholders equity after:*

– *adding back the average balance of goodwill impaired, amortised or previously written-off directly to reserves;*

– *deducting the average balance of HSBC s revaluation surplus relating to property held for own use. This reserve was generated when determining the deemed carrying cost of such properties on transition to IFRSs and will run down as the properties are sold;*

– *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.*

3 *Return on invested capital is based on the profit attributable to ordinary shareholders of the parent company adding back goodwill impaired.*

Ratios of earnings to combined fixed charges (and preference share dividends)

	Half-year to 30 June	Year ended 31 December				
	2008	2007	2006	2005	2004	2003
Ratios of earnings to combined fixed charges						

Ratios in accordance with IFRSs						
excluding interest on deposits	**6.11**	7.52	7.93	9.60	8.64	
including interest on deposits	**1.30**	1.34	1.41	1.59	1.86	
Ratios in accordance with UK GAAP						
excluding interest on deposits					8.07	7.41
including interest on deposits					1.81	1.80
Ratios of earnings to combined fixed charges and preference share dividends						
Ratios in accordance with IFRSs:						
excluding interest on deposits	**5.93**	6.96	7.22	9.16	8.64	
including interest on deposits	**1.30**	1.34	1.40	1.59	1.86	
Ratios in accordance with UK GAAP						
excluding interest on deposits					8.07	7.41
including interest on deposits					1.81	1.80

For the purpose of calculating the ratios, earnings consist of income from continuing operations before taxation and minority interests, plus fixed charges, and after deduction of the unremitted pre-tax income of associated undertakings. Fixed charges consist of total interest expense, including or excluding interest on deposits, as appropriate, preference share dividends, as applicable, and the proportion of rental expense deemed representative of the interest factor.

The above table contains ratios based on UK GAAP, HSBC s previous primary GAAP, which is not comparable to financial information based upon IFRSs, as explained in HSBC s 2004 IFRSs Comparative Financial Information published on 5 July 2004.

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Interim Management Report: Impact of Market Turmoil

Background and disclosure policy

During the summer of 2007, credit risk concerns emanating from the US sub-prime mortgage market triggered a widespread deterioration in the markets for securitised and structured financial assets, with consequent disruption to the global financial system. As a result, many institutions recorded considerable reductions in the fair values of their asset-backed securities (ABSs) and leveraged structured transactions, most significantly in those related to sub-prime mortgages, but also in other asset classes. As price observability for structured credit risk, including the prime tranches of such risk, became opaque, many markets for such assets became illiquid. The resulting constraint on the ability of financial institutions to access wholesale markets to fund such assets reduced capacity, adding further stress to all asset prices.

These market conditions continued in the first six months of 2008. In general, financial institutions took steps to reduce leveraged exposures, build liquidity and raise additional capital where necessary. However, money markets remained volatile, exhibiting wide interest spreads, and markets for securitised and structured financial assets continued to be highly constrained. This lack of market liquidity, together with the restricted availability of credit, contributed to general weakness in economic conditions in the US, UK, and Europe, in particular affecting housing and commercial property markets, and added to the difficult market conditions for such assets.

The deterioration in the fair value of assets supported by sub-prime mortgages continued in the first half of 2008 with the primary market for non-US government sponsored issues remaining weak. Spreads widened due to credit and liquidity concerns, and mortgage delinquencies continued to increase beyond the levels priced into securitisation issuance over the last few years. The impact continued to extend beyond sub-prime related assets, with the fair value of securities backed by Alt-A collateral (defined below), in particular, suffering a significant deterioration in fair value.

This section contains disclosures about the effect on HSBC s securitisation activities and structured products of the recent market turmoil.

Details of HSBC s principal exposure to the US and the UK mortgage markets, which primarily takes the form of credit risk from loans and advances to customers, are provided on page 161.

It is HSBC s policy to provide meaningful disclosures that help investors and other stakeholders understand the financial position, performance and changes in the financial position of the Group. Whenever appropriate, the Group provides information that goes beyond the minimum levels required by accounting standards, statutory and regulatory requirements and listing rules. In the specific context of the recent market turmoil in markets for securitised and structured assets, HSBC has considered the recent recommendations relating to disclosure contained within the report of the Financial Stability Forum on Enhancing Market and Institutional Resilience (April 2008) and the report by the Committee of European Banking Supervisors on Banks Transparency on Activities and Products Affected by the Recent Market Turmoil (June 2008) and, in addition, has considered feedback from investors and other stakeholders on the disclosures that investors would find most useful. As a result, HSBC has expanded certain disclosures provided in the *Annual Report and Accounts 2007* and included them in the *Interim Report 2008*.

The specific topics covered in respect of HSBC s securitisation activities and structured products are as follows:

- overview of exposure;
- business model;
- risk management;
- accounting policies;
- nature and extent of HSBC s exposures;

- fair values of financial instruments; and
- special purpose entities.

Overview of exposure

At 30 June 2008 the carrying value of HSBC s exposure to ABSs, trading loans held for securitisation plus the exposure to leveraged finance transactions was US$117 billion (31 December 2007: US$135 billion), summarised as follows:

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	At 30 June 2008		At 31 December 2007	
	Carrying value US$bn	**Percentage sub-prime and Alt-A %**	Carrying value US$bn	Percentage sub-prime and Alt-A %
Asset-backed securities				
fair value through profit or loss	**29**	**14**	32	20
available for sale[1]	**73**	**24**	85	28
held to maturity[1]	**3**	**6**	3	7
Total asset-backed securities	**105**	**21**	120	26
Trading loans	**4**	**93**	6	94
Leveraged finance[2]	**8**		9	
	117	**22**	135	27

1 *Total includes holdings of ABSs issued by Freddie Mac and Fannie Mae.*
2 *Includes the carrying amount of funded loans plus the net exposure to unfunded leveraged finance commitments.*

Most of these exposures are in the Global Banking and Markets business segment.

The total carrying value of ABSs on the balance sheet included ABS holdings of US$21.5 billion (31 December 2007: US$32.1 billion) in certain special purpose entities (SPEs), discussed further below, on which significant first loss risks are borne by external investors. At 30 June 2008, 23 per cent of the total carrying value of ABSs and trading loans held for securitisation, or US$25 billion, was in respect of sub-prime and Alt-A residential mortgage

exposure, of which US$7.7 billion was held through the SPEs referred to above.

Financial effect of market turmoil

The write-downs incurred by the Group on ABSs, structured and leveraged finance transactions, and the movement in fair values on available-for-sale ABSs taken to equity in the six months to 30 June, are summarised in the following table. Most of these effects were recorded in the Global Banking and Markets business segment.

	Half-year to	
	30 June 2008 US$bn	31 December 2007 US$bn
Write-downs taken to income statement	**(4.0)**	(2.3)
Fair value movement taken to available-for-sale reserve on ABSs in the period	**(6.1)**	(2.2)
Closing balance of available-for-sale reserve relating to ABSs	**(8.3)**	(2.2)

Further analysis of the write-downs taken to the income statement by Global Banking and Markets, and the net carrying amounts of these positions that have generated these write-downs, are shown in the following table.

Global Banking and Markets write-downs taken to the income statement and carrying values

	Write-downs at half-year to		Carrying values at	
	30 June 2008	31 December 2007	**30 June 2008**	31 December 2007
	US$m	US$m	**US$m**	US$m
Sub-prime mortgage-related assets				
loan securitisation	**301**	529	**1,565**	1,965
credit trading	**665**	463	**1,377**	1,700
Other ABSs	**1,327**	459	**8,923**	9,830
Derivative transactions with monolines				
investment grade counterparts	**598**	133	**1,206**	1,209
non-investment grade counterparts	**608**	214	**78**	
Leveraged finance[1]	**278**	195	**8,328**	8,742
Other credit related items	**99**	142		
Available-for-sale ABSs impairment	**55**			
	3,931	2,135		

1 *Includes the carrying amount of funded loans plus the net exposure to unfunded leveraged finance commitments.*

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Global Banking and Markets asset-backed securities classified as available-for-sale

HSBC s principal exposure to ABSs is in the Global Banking and Markets business through its exposure to structured investment vehicles (SIVs), the

Global Banking and Markets available-for-sale ABSs exposure

successor securities investment conduits (SICs), and positions held directly.

The table below summarises Global Banking and Markets exposures to ABSs held on an available-for-sale basis.

	Directly held US$m	SIVs and SICs US$m	Total US$m
Total carrying amount of net principal exposure	**48,372**	**21,359**	**69,731**
which includes sub-prime/Alt-A exposure	**9,376**	**7,721**	**17,097**
Available-for-sale reserves relating to sub-prime/Alt-A exposure	**(3,612)**	**(2,882)**	**(6,494)**
Impairment charge	**(55)**	**(134)**	**(189)**
Impairment charge borne by capital note holders		**134**	**134**
Impairment charge borne by HSBC	**(55)**		**(55)**

Structured investment vehicles and securities investment conduits

In the table above, the total carrying values of ABSs on the balance sheet in respect of SIVs and SICs represent holdings in which the significant first loss risks are borne by external investors, through the investors holdings of capital notes.

Capital notes issued by the successor SICs will suffer the initial losses from assets within these vehicles and the assets remaining in the SIVs until settlement. The maximum value of future impairment losses which may be borne by capital note holders is US$1.2 billion. Impairments borne by capital note holders at 30 June 2008 were US$134 million.

At each balance sheet date an assessment is made of whether there is any objective evidence of impairment in the value of a financial asset or group of assets in this category. Impairment charges incurred on assets held by consolidated SIVs and SICs excluding Solitaire Funding Limited (Solitaire) are matched by a credit to the impairment line for the amount of the loss borne by capital note holders.

The exposures attributable to Solitaire have been shown together with the directly held positions in recognition of the first loss protection of US$1.2 billion provided by HSBC through credit enhancement.

Impairments recognised at 30 June 2008 from assets held within Solitaire or directly by Global Banking and Markets were US$55 million, based on a notional principal value of securities which were impaired of US$88 million. The low level of impairment recognised in comparison to the deficit

in the available-for-sale reserve is a reflection of the credit quality and seniority of the assets.

Sub-prime and Alt-A residential mortgage-backed securities

Management s current assessment of the holdings of available-for-sale ABSs with the most sensitivity to possible future impairment is focused on sub-prime and Alt-A residential mortgage-backed securities (MBSs).

Excluding holdings in the SIVs and SICs discussed above, the Group s available-for-sale holdings in these categories amounted to US$9.4 billion at 30 June 2008 (31 December 2007: US$10.0 billion). During the six months to 30 June 2008, the movement in fair values of these securities taken to equity was a reduction of US$2.3 billion. The deficit in the available-for-sale fair value reserve as at 30 June 2008 in relation to these securities was US$3.6 billion. The main factor in the reduction in fair value of these securities over the period was the effect of reduced market liquidity and negative market sentiment. The level of actual credit losses experienced has been low to date, despite the deterioration in the performance of the underlying collateral for these securities in the period as US house prices fell and defaults increased.

Based on management s current assessment of the credit quality of these securities, including stressed scenarios for collateral defaults and house prices, and given the level of credit support available, management believes that the cost of future impairment losses which may emerge in respect of holdings of available-for-sale US sub-

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prime and Alt-A residential MBSs is likely to be modest in relation to the fair value deficit in the available-for-sale fair value reserve at 30 June 2008.

Business model

Asset-backed securities, structured products and leveraged acquisition finance

HSBC is or has been involved in the following activities in these areas:

- the purchase of US mortgage loans with the intention of structuring and placing securitisations into the market;
- trading in ABSs, including MBSs, in secondary markets;
- the holding of MBSs and other ABSs in balance sheet management activities, with the intention of earning net interest income over the life of the securities;
- the holding of MBSs and other ABSs as part of investment portfolios, including the SIVs, SICs and money market funds described under Special purpose entities below, with the intention of earning net interest income and management fees;
- MBSs or other ABSs held in the trading portfolio hedged through credit derivative protection, typically purchased from monoline insurers, with the intention of earning the spread differential over the life of the instruments; and
- leveraged acquisition finance: originating loans for the purposes of syndicating or selling them down in order to generate a trading profit and, to a lesser extent, holding them in order to earn interest margin over their lives.

Overall, these business activities were historically not a significant part of Global Banking and Markets business, and Global Banking and Markets was not reliant on the activities for any material aspect of its business operations or profitability.

The purchase and securitisation of US mortgage loans and the secondary trading of US MBSs was conducted in HSBC s US MBSs business. This business was discontinued in 2007.

Special purpose entities

HSBC enters into certain transactions with customers in the ordinary course of business which involve the establishment of SPEs to facilitate customer transactions. Some of these SPEs hold assets whose fair values have been adversely affected by recent market conditions.

SPEs are used in HSBC s business in order to provide structured investment opportunities for customers, facilitate the raising of funding for customers business activities, or diversify HSBC s sources of funding and/or improve capital efficiency.

The use of SPEs is not a significant part of HSBC s activities and HSBC is not reliant on the use of SPEs for any material part of its business operations or profitability. Detailed disclosures of HSBC s sponsored SPEs are provided on page 137.

Risk management

The effect of the recent market turmoil on HSBC s risk exposures, the way in which HSBC has managed risk exposures in this context, and any changes made in HSBC s risk management polices and procedures in response to the market conditions, are set out in the following sections:

- Liquidity risk The impact of market turmoil on the Group s liquidity risk position (see page 182).
- Market risk The impact of market turmoil on market risk (see page 184).

In addition to holdings of securitised and structured assets, HSBC also provides personal loans to customers in the US, a proportion of which are in the nature of sub-prime loans. HSBC s exposure to US personal loans and receivables is set out in the Risk section see Areas of special interest credit risk on page 161.

Accounting policies

HSBC s accounting policies regarding the classification and valuation of financial instruments are in accordance with the requirements of IAS 32 Financial Instruments: Presentation and IAS 39 Financial Instruments: Recognition and Measurement . HSBC has not made any changes to the accounting policies described on pages 347 to 361 of the *Annual Report and Accounts 2007*.

The following is a summary of certain key policies relevant to an understanding of the market turmoil disclosures:

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Assets held at fair value with movements in fair value recognised in the income statement: this category includes ABSs that are held for trading or that are designated at fair value through profit or loss, and direct lending positions held for trading. The majority of HSBC s holdings of these assets arise from securitisation and secondary market trading activity.

Both assets held for trading and assets designated at fair value through profit or loss, are recorded initially at fair value less transaction costs. Transaction costs are taken directly to the income statement. Subsequently, the fair values are remeasured, and gains and losses from changes in fair value are recognised in the income statement.

Assets are classified as held for trading if they have been acquired principally for the purpose of selling or repurchasing in the near term, or they form part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent pattern of short-term profit-taking. Assets, other than those held for trading, are designated at fair value through profit or loss if they meet one or more of the designation criteria set out on page 352 of the *Annual Report and Accounts 2007*, and are so designated by management. The fair value designation once made, is irrevocable.

Assets held at fair value with movements in fair value recognised in equity: this category includes ABSs that are classified as available-for-sale including asset holdings in consolidated SPEs such as securities investment vehicles and conduits.

These securities are initially measured at fair value plus direct and incremental transaction costs. They are subsequently remeasured at fair value, and changes therein are recognised in equity in the Available-for-sale fair value reserve until the securities are either sold, or impaired. When available-for-sale securities are sold, cumulative gains or losses previously recognised in equity are recognised in the income statement as Gains less losses from financial investments .

At each balance sheet date, an assessment is made of whether there is any objective evidence of impairment in the value of a financial asset or group of assets in this category.

Impairment losses are recognised if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a loss event) and that loss event (or events) has an impact on the estimated future cash flows of the asset that can be reliably estimated.

If the asset is impaired, the difference between the asset s acquisition cost and the current fair value, less any previous impairment, is removed from equity and recognised in the income statement. Any subsequent reduction in the fair value of an impaired asset is taken to the income statement.

Impairment losses for available-for-sale debt securities are recognised within Loan impairment charges and other credit risk provisions in the income statement and impairment losses for available-for-sale equity securities are recognised within Gains less losses from financial investments in the income statement.

Any impairment losses recognised in the income statement relating to ABSs are recorded in the income statement in the Loan impairment charges and other credit risk provisions line. Impairment losses incurred on assets held by consolidated securities investment vehicles and conduits are matched by a credit to the impairment line for the amount of the loss borne by capital note holders.

In a subsequent period, if the fair value of the debt security increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the income statement that indicates that the debt security is no longer impaired, the impairment loss may be reversed through the income statement. Impairment losses on available-for-sale equity securities are not reversed.

Assets held at amortised cost: a small proportion of HSBC s holdings of ABSs are held to maturity. These assets are initially recorded at fair value plus any directly attributable transaction costs and are subsequently measured at amortised cost using the effective interest method, less any impairment losses.

An analysis of ABSs and direct lending by balance sheet category is provided on page 118.

Leveraged finance: For certain leveraged finance and syndicated lending activities, HSBC may commit to underwrite loans on fixed contractual terms for specified periods of time, where the drawdown of the loan is contingent upon certain future events outside the control of HSBC. Where the loan arising from the lending commitment is expected to be held for trading, the commitment to lend is recorded as a trading derivative and measured at fair value through profit or loss. On drawdown, the loan is classified as held for trading, and measured at fair value through profit or loss.

Where it is not HSBC s intention to trade the loan, a provision on the loan commitment is only

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recorded where it is probable that HSBC will incur a loss. This may occur, for example, where a loss of principal is probable or the interest rate charged on the loan is lower than the cost of funding. On inception of the loan, the hold portion is recorded at its fair value. Where this fair value is lower than the cash amount advanced (for example, due to the rate of interest charged on the loan being below the market rate of interest), the write-down is charged to the income statement. The write-down will be recovered over the life of the loan, through the recognition of interest income using the effective interest rate method, unless the loan is or becomes impaired. The write-down is recorded as a reduction to other operating income.

An analysis of HSBC s leveraged finance lending activity and its exposure to leveraged finance transactions through holdings of ABSs that are supported by leveraged finance-related collateral, is provided on page 127. The accounting policy for these securities is consistent with holdings of other ABSs described above.

Nature and extent of HSBC s exposures

This section contains information on HSBC s exposures to direct lending held at fair value through profit or loss, ABSs including MBSs and collateralised debt obligations (CDOs), monoline insurers and leveraged finance transactions.

MBSs are securities that represent an interest in a group of mortgages. Investors in these securities have the right to receive future mortgage payments (interest and/or principal). Where an MBS references mortgages with different risk profiles, the MBS is classified according to the highest risk class. Consequently, an MBS with both sub-prime and Alt-A exposures is classified as sub-prime.

CDOs are securities in which ABSs and/or certain other related assets have been purchased and securitised by a third party, or securities which pay a return which is referenced to those assets. CDOs may feature exposure to sub-prime mortgage assets through the underlying assets. As there is often uncertainty surrounding the nature of the underlying collateral supporting CDOs, all CDOs supported by residential mortgage-related assets, irrespective of the level of sub-prime assets, are classified as sub-prime.

HSBC s holdings of ABSs and CDOs, and its direct lending positions, include the following categories of collateral and lending activity:

- **sub-prime**: loans to customers who have limited credit histories, modest incomes, high debt-to-income ratios or have experienced credit problems caused by occasional delinquencies, prior charge-offs, bankruptcy or other credit- related actions. For US mortgages, US credit scores are primarily used to determine whether a loan is sub-prime. US home equity lines of credit are classified as sub-prime. For non-US mortgages, management judgement is used to identify loans of similar risk characteristics to sub-prime, for example, UK non-conforming mortgages (see below);

- **US home equity lines of credit (HELOCs)**: a form of revolving credit facility provided to customers, which is supported by a first or second lien charge over residential property;

- **US Alt-A**: loans classified as Alt-A are regarded as lower risk than sub-prime, but they share higher risk characteristics than lending under normal criteria. US credit scores, as well as the level of mortgage documentation held (such as proof of income), are considered when determining whether an Alt-A classification is appropriate. Non-agency mortgages in the US are classified as Alt-A if they do not meet the criteria for classification as sub-prime. These are mortgages not eligible to be sold to the major US government agency, Ginnie Mae (Government National Mortgage Association), and government sponsored enterprises in the mortgage market, Fannie Mae (the Federal National Mortgage Association) and Freddie Mac (the Federal Home Loan Mortgage Corporation);

- **US government agency mortgage-related assets**: securities that are guaranteed by US Government agencies, such as Ginnie Mae;

- **US Government sponsored enterprises mortgage-related assets**: securities that are guaranteed by US Government sponsored entities, including Fannie Mae and Freddie Mac;

- **UK non-conforming mortgage-related assets**:
UK mortgages that do not meet normal lending criteria. This includes instances where the normal level of documentation has not been provided (for example, in the case of self- certification of income), or where increased risk factors, such as poor credit history, result in lending at a rate that is higher than the normal lending rate. UK non-conforming mortgages are treated as sub-prime exposures; and

- **other mortgage-related assets**: residential mortgage-related assets that do not meet any of

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the classifications described above. Prime residential mortgage-related assets are included in this category.

HSBC s exposure to non-residential mortgage-related ABSs and direct lending includes:

- **commercial property mortgage-related assets**: MBSs with collateral other than residential mortgage-related assets;
- **leveraged finance-related assets**: securities with collateral relating to leveraged finance loans;

student loan-related assets: securities with collateral relating to student loans; and

other assets: securities with other receivable- related collateral.

Carrying amount of HSBC s consolidated holdings of ABSs, and direct lending held at fair value through profit or loss

	At 30 June 2008					
	Trading US$m	Available for sale US$m	Held to maturity US$m	Designated at fair value through profit or loss US$m	Total US$m	Of which: held through consolidated SPEs US$m
Sub-prime residential mortgage-related assets	5,914	6,935		2	12,851	7,328
Direct lending	3,534				3,534	1,825
MBSs and MBS CDOs[1]	2,380	6,935		2	9,317	5,503
US Alt-A residential mortgage-related assets	2,084	10,316	165		12,565	7,199
Direct lending	325				325	
MBSs[1]	1,759	10,316	165		12,240	7,199
US government agency mortgage-related assets MBSs[1]	181	6,299	535		7,015	
US government-sponsored enterprises mortgage-related assets MBSs[1]	2,008	13,994	1,947	25	17,974	
Other residential mortgage-related assets	3,320	5,625		61	9,006	3,531
Direct lending	298				298	
MBSs[1]	3,022	5,625		61	8,708	3,531
Commercial property mortgage-related assets	3,265	10,369		101	13,735	7,741
Direct lending						
MBSs and MBS CDOs[1]	3,265	10,369		101	13,735	7,741
Leveraged finance-related assets						
ABSs and ABS CDOs[1]	259	5,613			5,872	4,666
Student loan-related assets						

ABSs and ABS CDOs[1]	**175**	**6,262**		**4**	**6,441**	**5,407**
Other assets	**8,262**	**7,410**		**7,310**	**22,982**	**4,862**
Direct lending						
ABSs and ABS CDOs[1]	**8,262**	**7,410**		**7,310**	**22,982**	**4,862**
	25,468	**72,823**	**2,647**	**7,503**	**108,441**	**40,734**

For footnotes, see page 128.

The above table excludes leveraged finance transactions, which are shown separately on page 127.

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	At 31 December 2007					
	Trading	Available for sale	Held to maturity	Designated at fair value through profit or loss	Total	Of which: held through consolidated SPEs
	US$m	US$m	US$m	US$m	US$m	US$m
Sub-prime residential mortgage-related assets	9,431	9,311		2	18,744	11,504
Direct lending	5,825				5,825	3,596
MBSs and MBS CDOs[1]	3,606	9,311		2	12,919	7,908
US Alt-A residential mortgage-related assets	3,288	14,760	173		18,221	11,193
Direct lending	342				342	
MBSs[1]	2,946	14,760	173		17,879	11,193
US government agency mortgage-related assets MBSs[1]	204	5,239	552		5,995	
US government-sponsored enterprises mortgage-related assets MBSs[1]	2,583	11,414	1,881	26	15,904	
Other residential mortgage-related assets	5,243	5,701		289	11,233	4,441
Direct lending	416				416	
MBSs[1]	4,827	5,701		289	10,817	4,441
Commercial property mortgage-related assets	3,467	10,505		105	14,077	8,600
Direct lending						
MBSs and MBS CDO[1]	3,467	10,505		105	14,077	8,600
Leveraged finance-related assets						
ABSs and ABS CDOs[1]	263	5,820			6,083	5,126
Student loan-related assets						
ABSs and ABS CDOs[1]	144	7,052			7,196	6,308
Other assets	6,252	14,784		7,736	28,772	13,596
Direct lending	3				3	
ABSs and ABS CDOs[1]	6,249	14,784		7,736	28,769	13,596
	30,875	84,586	2,606	8,158	126,225	60,768

For footnotes, see page 128.

Included in the above table are ABSs which are held through SPEs that are consolidated by HSBC. Although HSBC includes these assets in full on its balance sheet, the risks arising from the assets are mitigated to the extent of third party investment in notes issued by those SPEs. For a description of HSBC s holdings of and arrangements with SPEs, see page 137.

The exposure detailed above includes long positions matched by specific credit derivatives with monolines and other financial institutions. These positions comprise:

- residential MBSs with a carrying value of US$1.5 billion (31 December 2007: US$2.1 billion);
- residential MBS CDOs with a carrying value of US$174 million (31 December 2007: US$349 million); and
- ABSs other than residential MBSs and MBS CDOs with a carrying value of US$11.6 billion (31 December 2007: US$10.8 billion).

In the tables which follow, carrying amounts and gains and losses are given for securities except those matched by specific credit derivatives with monolines. The counterparty credit risk arising from the derivative transactions undertaken with monoline insurers is included in the monoline exposure analysis on page 126.

US government-sponsored enterprises mortgage-related assets shown in the table above include holdings of securities issued by Freddie Mac of US$9.4 billion (31 December 2007: US$6.8 billion) and by Fannie Mae of US$7.4 billion (31 December 2007: US$8.5 billion).

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HSBC s consolidated holdings of US ABSs, and direct lending held at fair value through profit or loss

	Half-year to 30 June 2008				At 30 June 2008				At 3	
	Unrealised gains and (losses)[3] US$m	**Realised gains and (losses)[4] US$m**	**Fair value movements through equity[5] US$m**	**Impairment[6] US$m**	**Gross principal[7] US$m**	**CDS gross protection[8] US$m**	**Net principal exposure[9] US$m**	**Carrying amount[10] US$m**	Gross principal[7] US$m	prote U
US sub-prime residential mortgage-related assets										
Direct lending	**(234)**	**(8)**			**4,199**		**4,199**	**3,534**	6,288	
MBSs[1]	**(621)**	**6**	**(903)**	**(29)**	**8,239**	**601**	**7,638**	**5,283**	9,576	
high grade[2]	**(228)**	**7**	**(518)**	**(29)**	**5,930**	**571**	**5,359**	**4,142**	9,079	
rated C to A	**(333)**		**(385)**		**2,292**	**30**	**2,262**	**1,118**	462	
not publicly rated	**(60)**	**(1)**			**17**		**17**	**23**	35	
MBS CDOs[1]	**(123)**		**(32)**	**(21)**	**1,200**	**569**	**631**	**152**	1,157	
high grade[2]	**(8)**		**(32)**		**230**	**50**	**180**	**97**	923	
rated C to A	**(115)**			**(21)**	**970**	**519**	**451**	**55**	234	
not publicly rated										
	(978)	**(2)**	**(935)**	**(50)**	**13,638**	**1,170**	**12,468**	**8,969**	17,021	
US Alt-A residential mortgage-related assets										
Direct lending					**329**		**329**	**325**	341	
MBSs[1]	**(368)**	**(59)**	**(3,243)**	**(5)**	**17,548**	**204**	**17,344**	**11,349**	19,175	
high grade[2]	**(340)**	**(49)**	**(3,115)**	**(5)**	**16,898**	**204**	**16,694**	**10,969**	19,099	
rated C to A	**(29)**	**(9)**	**(100)**		**533**		**533**	**299**	64	
not publicly rated	**1**	**(1)**	**(28)**		**117**		**117**	**81**	12	
	(368)	**(59)**	**(3,243)**	**(5)**	**17,877**	**204**	**17,673**	**11,674**	19,516	
US government agency mortgage-related assets										
MBSs[1]	**(2)**		**(54)**		**7,052**		**7,052**	**7,015**	5,996	
high grade[2]	**(2)**		**(54)**		**7,052**		**7,052**	**7,015**	5,996	
rated C to A										
not publicly rated										
US government-sponsored enterprises mortgage-related assets										

MBSs[1]	**(50)**	**40**	**(91)**		**18,249**		**18,249**	**17,974**	16,125
high grade[2]	**(50)**	**40**	**(91)**		**18,249**		**18,249**	**17,974**	16,125
rated C to A									
not publicly rated									
Balance carried forward	**(1,398)**	**(21)**	**(4,323)**	**(55)**	**56,816**	**1,374**	**55,442**	**45,632**	58,658

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HSBC s consolidated holdings of US ABSs, and direct lending held at fair value through profit or loss (continued)

	Half-year to 30 June 2008				At 30 June 2008				At 31 Decem	
	Unrealised gains and (losses)[3] US$m	Realised gains and (losses)[4] US$m	Fair value movements through equity[5] US$m	Impairment[6] US$m	Gross principal[7] US$m	CDS gross protection[8] US$m	Net principal exposure[9] US$m	Carrying amount[10] US$m	Gross principal[7] US$m	CDS gross protection[8] US$m
Balance brought forward	(1,398)	(21)	(4,323)	(55)	56,816	1,374	55,442	45,632	58,658	1,514
Other US residential mortgage-related assets										
Direct lending	(26)	34			312		312	298	424	
MBSs[1]	(107)	(123)	(4)		889	195	694	555	1,587	821
high grade[2]	(105)	(123)	(4)		864	187	677	546	1,565	799
rated C to A	(2)				25	8	17	9	22	22
not publicly rated										
	(133)	(89)	(4)		1,201	195	1,006	853	2,011	821
Commercial property mortgage-related assets										
MBS and MBS CDOs[1]	(69)		(295)		5,838	415	5,423	4,943	5,981	685
high grade[2]	(55)		(290)		5,554	415	5,139	4,682	5,760	685
rated C to A			(5)		64		64	55		
not publicly rated	(14)				220		220	206	221	
Leveraged finance-related assets										
ABSs and ABS CDOs[1]	(4)		(227)		5,153	577	4,576	4,168	4,930	322
high grade[2]	(4)		(227)		5,153	577	4,576	4,168	4,930	322
rated C to A										
not publicly rated										
Student loan-related assets										
ABSs and ABS CDOs[1]	(64)		(507)		7,412		7,412	6,437	7,352	
high grade[2]	(44)		(437)		7,202		7,202	6,343	7,312	
rated C to A	(20)		(70)		210		210	94	40	

not publicly rated											
Other assets											
ABS and ABS CDOs[1]	**(186)**	**(3)**	**(27)**		**9,057**	**2,941**	**6,116**	**4,956**	10,476	2,735	
high grade[2]	**(111)**	**(2)**	**6**		**6,345**	**2,433**	**3,912**	**3,086**	9,353	2,707	
rated C to A	**(62)**	**(1)**	**(56)**		**1,874**	**508**	**1,366**	**1,076**	1,008	28	
not publicly rated	**(13)**		**23**		**838**		**838**	**794**	115		
Total	**(1,854)**	**(113)**	**(5,383)**	**(55)**	**85,477**	**5,502**	**79,975**	**66,989**	89,408	6,077	

For footnotes, see page 128.

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HSBC s consolidated holdings of UK ABSs, and direct lending held at fair value through profit or loss

Half-year to 30 June 2008			At 30 June 2008	At 31 December 2007
Unrealised	Realised	Fair value		