

The Hongkong and Shanghai Banking Corporation Limited Annual Results for 2021

Consolidated Income Statement for the Year Ended 31 December 2021

	2021 HK\$m	2020 HK\$m
Net interest income	98,113	111,513
interest income	121,382	147,376
interest expense	(23,269)	(35,863)
Net fee income	45,296	41,670
fee income	57,819	52,370
fee expense	(12,523)	(10,700)
Net income from financial instruments held for trading or managed on a fair value basis	28,359	32,172
Net income from assets and liabilities of insurance businesses, including related derivatives, measured at fair value through profit or loss	18,180	13,128
Changes in fair value of designated debts issued and related derivatives	(639)	(171)
Changes in fair value of other financial instruments mandatorily measured at fair value through profit or loss	(25)	138
Gains less losses from financial investments	1,667	1,624
Net insurance premium income	61,722	61,563
Other operating income	2,033	5,612
Total operating income	254,706	267,249
Net insurance claims and benefits paid and movement in liabilities to policyholders	(76,048)	(77,911)
Net operating income before change in expected credit losses and other credit impairment charges	178,658	189,338
Change in expected credit losses and other credit impairment charges	(6,539)	(17,719)
Net operating income	172,119	171,619
Employee compensation and benefits	(39,261)	(36,183)
General and administrative expenses	(52,327)	(46,304)
Depreciation and impairment of property, plant and equipment	(8,891)	(9,405)
Amortisation and impairment of intangible assets	(4,397)	(3,936)
Total operating expenses	(104,876)	(95,828)
Operating profit	67,243	75,791
Share of profit in associates and joint ventures	19,320	14,405
Profit before tax	86,563	90,196
Tax expense	(14,015)	(14,505)
Profit for the year	72,548	75,691
Attributable to:		
– ordinary shareholders of the parent company	64,633	66,997
– other equity holders	2,715	2,450
– non-controlling interests	5,200	6,244
Profit for the year	72,548	75,691

Consolidated Balance Sheet at 31 December 2021

	2021 HK\$m	2020 HK\$m
ASSETS		
Cash and balances at central banks	276,857	347,999
Items in the course of collection from other banks	21,632	21,943
Hong Kong Government certificates of indebtedness	332,044	313,404
Trading assets	777,450	600,414
Derivatives	365,167	422,945
Financial assets designated and otherwise mandatorily measured at fair value through profit or loss	202,399	178,960
Reverse repurchase agreements – non-trading	803,775	520,344
Loans and advances to banks	432,247	403,884
Loans and advances to customers	3,840,939	3,668,681
Financial investments	2,051,575	2,175,432
Amounts due from Group companies	112,719	83,203
Interests in associates and joint ventures	188,485	168,754
Goodwill and intangible assets	95,181	89,968
Property, plant and equipment	129,827	128,537
Deferred tax assets	3,353	3,325
Prepayments, accrued income and other assets	269,743	288,610
Total assets	9,903,393	9,416,403
LIABILITIES		
Hong Kong currency notes in circulation	332,044	313,404
Items in the course of transmission to other banks	25,701	25,669
Repurchase agreements – non-trading	255,374	136,157
Deposits by banks	280,310	248,628
Customer accounts	6,177,182	5,911,396
Trading liabilities	92,723	60,812
Derivatives	355,791	428,211
Financial liabilities designated at fair value	138,965	167,013
Debt securities in issue	67,364	79,419
Retirement benefit liabilities	1,890	2,701
Amounts due to Group companies	356,233	296,308
Accruals and deferred income, other liabilities and provisions	219,206	215,987
Liabilities under insurance contracts	638,145	581,406
Current tax liabilities	2,378	2,669
Deferred tax liabilities	32,522	30,997
Subordinated liabilities	4,054	4,065
Total liabilities	8,979,882	8,504,872
EQUITY		
Share capital	172,335	172,335
Other equity instruments	44,615	44,615
Other reserves	151,804	149,500
Retained earnings	488,055	478,903
Total shareholders' equity	856,809	845,353
Non-controlling interests	66,702	66,178
Total equity	923,511	911,531
Total liabilities and equity	9,903,393	9,416,403

Capital Adequacy Ratios

The following table shows the capital ratios as contained in the 'Capital Adequacy Ratio' return submitted to the HKMA on a consolidated basis under the requirements of section 3C(1) of the Banking (Capital) Rules.

	At 31 December 2021 %	At 31 December 2020 %
Common equity tier 1 ('CET1') capital ratio	15.4	17.2
Tier 1 capital ratio	16.8	18.8
Total capital ratio	18.7	20.8

Board of Directors

Peter Tung Shun Wong, GBS, JP, <i>Non-executive Chairman</i>	Rajnish Kumar*
David Gordon Eldon, GBS, CBE, JP, <i>Non-executive Deputy Chairman</i>	Beau Khoo Chen Kuok*
David Yi Chien Liao [†]	Irene Yun-lien Lee*
Surendranath Ravi Roshia [†]	Victor Tzar Kuoi Li*
Graham John Bradley*	Ewen James Stevenson*
Dr Christopher Wai Chee Cheng*, GBS, OBE	Kevin Anthony Westley*, BBS
Sonia Chi Man Cheng*	Tan Sri (Sir) Francis Sock Ping Yeoh*, KBE, CBE
Yiu Kwan Choi*	

* Independent non-executive Director

[†] Non-executive Director

[†] Co-Chief Executive Officer

Independent Auditor's Report to the Shareholder of The Hongkong and Shanghai Banking Corporation Limited (incorporated in Hong Kong with limited liability)

Opinion

What we have audited

The consolidated financial statements of The Hongkong and Shanghai Banking Corporation Limited (the 'Bank') and its subsidiaries (the 'group'), which are set out on pages 73 to 131, comprise:

- the consolidated balance sheet as at 31 December 2021;
- the consolidated income statement for the year then ended;
- the consolidated statement of comprehensive income for the year then ended;
- the consolidated statement of changes in equity for the year then ended;
- the consolidated statement of cash flows for the year then ended; and
- the notes¹ on the consolidated financial statements, which include significant accounting policies and other explanatory information.

¹ Certain required disclosures as described in Note 1.1(d) on the consolidated financial statements have been presented elsewhere in the Annual Report and Accounts 2021, rather than in the notes on the consolidated financial statements. These are cross-referenced from the consolidated financial statements and are identified as audited.

Our opinion

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of the group as at 31 December 2021, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with Hong Kong Financial Reporting Standards ('HKFRSs') issued by the Hong Kong Institute of Certified Public Accountants ('HKICPA') and have been properly prepared in compliance with the Hong Kong Companies Ordinance.

Basis for Opinion

We conducted our audit in accordance with Hong Kong Standards on Auditing ('HKSA's') issued by the HKICPA. Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Consolidated Financial Statements section of our report.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Independence

We are independent of the group in accordance with the HKICPA's Code of Ethics for Professional Accountants ('the Code'), and we have fulfilled our other ethical responsibilities in accordance with the Code.

Key Audit Matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matters identified in our audit are summarised as follows:

- Allowances for expected credit losses on loans and advances to customers
- Impairment assessment of investment in associate – Bank of Communications Co., Limited ('BoCom')
- The present value of in-force long-term insurance business ('PVIF') and liabilities under non-linked life insurance contracts

Allowances for the expected credit losses on loans and advances to customers

Nature of the Key Audit Matter

At 31 December 2021, the group recorded allowances for expected credit losses ('ECL') on loans and advances to customers of HK\$32.0bn.

The determination of the ECL on loans and advances to customers requires the use of complex credit risk methodologies that are applied in models using the group's historic experience of the correlations between defaults and losses, borrower creditworthiness, segmentation of customers or portfolios and economic conditions.

It also requires the determination of assumptions which involve estimation uncertainty. The assumptions that we focused our audit on include those with greater levels of management judgement and for which variations have the most significant impact on ECL on loans and advances to customers. Specifically, these included economic scenarios and their likelihood, as well as customer risk ratings. Likewise, there is inherent uncertainty with the consensus economic forecast data from external economists as well as the prospects of future recoverability of credit impaired wholesale exposures.

The progression of the Covid-19 pandemic and other current macroeconomic conditions impact the inherent risk and estimation uncertainty involved in determining the ECL on loans and advances to customers.

Management judgemental adjustments to ECL on loans and advances to customers therefore continue to be made. This includes judgemental adjustments to the ECL for certain wholesale sectors, as well as adjustments related to the retail portfolio.

Matters discussed with the Audit Committee

We discussed the appropriateness of the methodologies, their application, significant assumptions and related disclosures with the Audit Committee, giving consideration to the current macroeconomic conditions. This included management judgemental adjustments made to derive the ECL on loans and advances to customers. We further discussed the governance and controls over the process in determining ECL on loans and advances to customers.

How our audit addressed the Key Audit Matter

We tested controls in place over the methodologies, their application, significant assumptions and data used to determine the ECL on loans and advances to customers. These included controls over:

- Model development, validation and monitoring;
- Approval of economic scenarios;
- Approval of the probability weightings assigned to economic scenarios;
- Assigning customer risk ratings;
- Approval of management judgemental adjustments; and
- Review of input and assumptions applied in estimating the recoverability of credit-impaired wholesale exposures.

We performed substantive audit procedures over the compliance of ECL methodologies with the requirements of HKFRS 9. We engaged professionals with experience in ECL modelling to assess the appropriateness of changes to models during the year, and for a sample of those models, independently reperformed the modelling for certain aspects of the ECL calculation. We also assessed the appropriateness of methodologies and related models that did not change during the year.

We further performed the following to assess the significant assumptions and data:

- We challenged the appropriateness of the significant assumptions;
- We involved our economic experts in assessing the reasonableness of the severity and likelihood of certain economic scenarios;
- We tested a sample of customer risk ratings assigned to wholesale exposures; and
- We have independently assessed other significant assumptions and obtained corroborating evidence.

For a sample of management judgemental adjustments, we challenged the appropriateness of these and assessed the ECL determined.

We further considered whether the judgements made in selecting the significant assumptions and determining the management judgemental adjustments would give rise to indicators of possible management bias.

We assessed the adequacy of the disclosures in relation to ECL on loans and advances to customers made in the consolidated financial statements in the context of the applicable financial reporting framework.

Relevant references in the consolidated financial statements

Risk: Credit Risk, as cross-referenced from the consolidated financial statements (only information identified as audited), page 29-50

Note 1.2 (i) on the consolidated financial statements: Basis of preparation and significant accounting policies - Impairment of amortised cost and FVOCI financial assets, page 83-86



Note 2 (e) on the consolidated financial statements: Operating profit – Change in expected credit losses and other credit impairment charges, page 91

Note 10 on the consolidated financial statements: Loans and advances to customers, page 99

Impairment assessment of investment in associate – Bank of Communications Co., Limited ('BoCom')

Nature of the Key Audit Matter

At 31 December 2021, the fair value of the investment in BoCom, based on the share price, was HK\$118.2bn lower than the carrying value ('CV') of HK\$184.8bn. This is an indicator of potential impairment. An impairment test was performed, with supporting sensitivity analysis, using a value in use ('VIU') model. The VIU was HK\$8.2bn in excess of the CV. On this basis, no impairment was recorded.

The methodology applied in the VIU model is dependent on various assumptions, both short term and long term in nature. These assumptions, which are subject to estimation uncertainty, are derived from a combination of management's judgement, analysts' forecasts, market data or other relevant information.

The assumptions that we focused our audit on were those with greater levels of management judgement and subjectivity, and for which variations had the most significant impact on the VIU. Specifically, these included the discount rate, operating income growth rate, long-term profit and asset growth rates, cost-income ratio, expected credit losses, effective tax rates, and capital requirements (including Capital Adequacy Ratio, Tier 1 Capital Adequacy ratio and risk-weighted assets as a percentage of total assets).

Matters discussed with the Audit Committee

We discussed the appropriateness of the methodology, its application and significant assumptions with the Audit Committee. We also discussed the disclosures made in relation to BoCom, including the use of sensitivity analysis to explain estimation uncertainty and the changes in certain assumptions that would result in the VIU being equal to the CV.

How our audit addressed the Key Audit Matter

We tested controls in place over significant assumptions, the methodology and its application used to determine the VIU. We assessed the appropriateness of the methodology used, its application, and the mathematical accuracy of the calculations. In respect of the significant assumptions, we performed the following:

- Challenged the appropriateness of the significant assumptions and, where relevant, their interrelationships;
- Obtained corroborating evidence for data supporting significant assumptions that may include historic experience, external market information, third-party sources including analyst reports, information from BoCom management and historical publicly available BoCom financial information;
- Determined a reasonable range for the discount rate assumption, with the assistance of our valuation experts, and compared it to the discount rate used by management; and
- Assessed whether the judgements made in selecting the significant assumptions give rise to indicators of possible management bias.

We observed the meetings in March, May, September and November 2021 between management and BoCom management, held specifically to identify facts and circumstances impacting significant assumptions relevant to the determination of the VIU.

Representations were obtained from the Bank that assumptions used were consistent with information currently available to the Bank.

We assessed the adequacy of the disclosures in relation to BoCom made in the consolidated financial statements in the context of the applicable financial reporting framework.

Relevant references in the consolidated financial statements

Note 1.2 (a) on the consolidated financial statements: Basis of preparation and significant accounting policies - Consolidated and related policies, page 80-81

Note 14 on the consolidated financial statements: Interests in associates and joint ventures, page 102-105

The present value of in-force long-term insurance business ('PVIF') and liabilities under non-linked life insurance contracts

Nature of the Key Audit Matter

At 31 December 2021, the group has recorded an asset for PVIF of HK\$63.8bn and liabilities under non-linked life insurance contracts of HK\$608.5bn.

The determination of these balances requires the use of complex actuarial methodologies that are applied in models and involves judgement about future outcomes. Specifically, judgement is required in deriving the economic and non-economic assumptions. These assumptions are subject to estimation uncertainty, both for PVIF asset and the liabilities under non-linked life insurance contracts.

Matters discussed with the Audit Committee

We discussed the appropriateness of the methodologies, their application, significant assumptions and related disclosures with the Audit Committee. In relation to assumptions, we focused on those for which variations had the most significant impact on the valuation of PVIF and liabilities under non-linked life insurance contracts carrying value.

How our audit addressed the Key Audit Matter

We tested controls in place over the methodologies, their application, significant assumptions and data for PVIF asset and the liabilities under non-linked life insurance contracts. Specifically, these included controls over:

- policy data reconciliations from the policyholder administration system to the actuarial valuation system;
- assumptions setting;
- review and determination of methodologies used, and its application in models; and
- results aggregation and analysis processes.

With the assistance of our actuarial experts, we performed the following additional audit procedures to assess the methodologies used, their application, significant assumptions, data and disclosures:

- We assessed the appropriateness of the methodologies used, their application and the mathematical accuracy of the calculations;
- We challenged the appropriateness of the significant assumptions and, where relevant, their interrelationships. We have independently assessed these assumptions and obtained relevant corroborating evidence. We further considered whether the judgements made in selecting the significant assumptions would give rise to indicators of possible management bias;
- We performed substantive audit procedures over critical data used in the determination of these balances to ensure these are relevant and reliable; and
- We assessed the adequacy of the disclosures in relation to the asset for PVIF and liabilities under non-linked life insurance contracts made in the consolidated financial statements in the context of the applicable financial reporting framework.

Relevant references in the consolidated financial statements

Risk: Insurance manufacturing operations risk, as cross-referenced from the consolidated financial statements (only information identified as audited), page 62-66

Note 1.2 (j) on the consolidated financial statements: Basis for preparation and significant accounting policies - Insurance contracts, page 87

Note 3 on the consolidated financial statements: Insurance business, page 92

Note 15 on the consolidated financial statements: Goodwill and intangible assets, page 105-106

Other Information

The directors of the Bank are responsible for the other information. The other information comprises all of the information included in the Annual Report and Accounts 2021, Banking Disclosure Statement as at 31 December 2021 and List of the directors of the Bank's subsidiary undertakings (during the period from 1 January 2021 to 22 February 2022) other than the consolidated financial statements and our auditor's report thereon. We have obtained some of the other information including Certain defined terms, Cautionary statement regarding forward-looking statements, Chinese translation, Financial Highlights, Report of the Directors, Financial Review, Risk and Statement of Directors' Responsibilities sections of the Annual Report and Accounts 2021 prior to the date of this auditor's report. The remaining other information, including Banking Disclosure Statement as at 31 December 2021 and List of the directors of the Bank's subsidiary undertakings (during the period from 1 January 2021 to 22 February 2022), is expected to be made available to us after that date. The other information does not include the specific information presented therein that is identified as being an integral part of the consolidated financial statements and, therefore, covered by our audit opinion on the consolidated financial statements.

Our opinion on the consolidated financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

If, based on the work we have performed on the other information that we obtained prior to the date of this auditor's report, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

When we read the remaining other information, if we conclude that there is a material misstatement therein, we are required to communicate the matter to the Audit Committee and take appropriate action considering our legal rights and obligations.

Responsibilities of Directors and the Audit Committee for the Consolidated Financial Statements

The directors of the Bank are responsible for the preparation of the consolidated financial statements that give a true and fair view in accordance with HKFRSs issued by the HKICPA and the Hong Kong Companies Ordinance, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the directors are responsible for assessing the group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the group or to cease operations, or have no realistic alternative but to do so.

The Audit Committee is responsible for overseeing the group's financial reporting process.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. We report our opinion solely to you, as a body, in accordance with Section 405 of the Hong Kong Companies Ordinance and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with HKSA's will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with HKSA's, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the Audit Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, actions taken to eliminate threats or safeguards applied.

From the matters communicated with the Audit Committee, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor's report is Lars Christian Jordy Nielsen.

PricewaterhouseCoopers

Certified Public Accountants
Hong Kong, 22 February 2022

Annual Report and Accounts

The consolidated Balance Sheet and consolidated Income Statement printed above are extracted from the 2021 Annual Report and Accounts of The Hongkong and Shanghai Banking Corporation Limited. The notes form an integral part of the audited financial statement and a full understanding of the statements cannot be achieved without reference to the complete set of financial statements. Copies of the 2021 Annual Report and Accounts are available for viewing at the website www.hsbc.com.hk.

Name of all Subsidiary Companies of the Bank

A list of the Bank's subsidiaries is exhibited in the Bank's branches in Singapore. The list of subsidiaries can be made available upon request from: Corporate Governance & Secretariat Department, 10 Marina Boulevard, Marina Bay Financial Centre, Tower 2 #48-01, Singapore 018983.

Deposits

The laws in the country of incorporation of the Bank (the "Home Country") do not require the Bank to confer lower priority to the depositors of its foreign offices, vis-à-vis its Home Country depositors, in the repayment of deposits in the event of receivership, winding up proceedings or equivalent proceedings of the Bank.

