HSBC, Bangladesh

Disclosures on risk based capital
under Pillar - III of Base III
for the year ended 31 December 2018

HSBC

HSBC

The Hongkong and Shanghai Banking Corporation Limited Bangladesh Branch

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1 Disclosure policy

The following detailed qualitative and quantitative disclosures are provided in accordance with Bangladesh Bank rules and Basel III capital regulation under BRPD Circular no. 18 (21 December 2014). The purpose of these requirements is to complement the capital adequacy requirements and the Pillar III – supervisory review process. These disclosures are intended for market participants to assess key information about the Bank's exposure to various risks and to provide a consistent and understandable disclosure framework as per regulatory requirement. The Bank complies with the disclosure requirements set out by the Bangladesh Bank and International Financial Reporting Standards (IFRS) and International Accounting Standards (IAS) as approved by the Institute of Chartered Accountants of Bangladesh (ICAB).

The major highlights of the Bangladesh Bank regulations are:

- To maintain Capital Adequacy Ratio (CAR) at a minimum of 11.875% (including capital conservation buffer @1.875%) of Risk Weighted Assets (RWA);
- To adopt the standardised approach for credit risk for implementing Basel III, using national discretion for:
  - adopting the credit rating agencies as External Credit Assessment Institutions (ECAI) for claims on sovereigns and banks;
  - adopting simple/comprehensive approach for Credit Risk Mitigation (CRM).
  - all unrated corporate exposures are risk weighted by assigning a risk weighting of 125%.
- To adopt the standardised approach for market risk and basic indicator approach for operational risk.
- Capital adequacy returns must be submitted to Bangladesh Bank on a quarterly basis.

2 Scope of application

The Bank has no subsidiaries or significant investments and Basel III is applied at Bank level only.

3 Capital structure

Qualitative disclosures:

HSBC Bangladesh's capital structure consists of Tier I and Tier II capital which is align with regulatory capital structure. Tier I capital further categorised as Common Equity Tier 1 (CET1) and Additional Tier 1 capital. The computation of the amount of Common Equity Tier I, Additional Tier I and Tier II capital shall be subject to the following conditions:

- The Bank has to maintain at least 4.5% of total Risk Weighted Assets (RWA) as Common Equity Tier I capital.
- Tier I capital will be at least 6% of the total RWA.
- Minimum Capital to Risk-weighted Asset Ratio (CRAR) will be 10% of the total RWA.
- Additional Tier I capital can be maximum up to 1.5% of the total RWA or 33.33% of CET 1, whichever is higher.
- Tier II capital can be maximum up to 4% of the total RWA or 88.89% of CET1, whichever is higher.
- In addition to minimum CRAR, Capital Conservation Buffer (CCB) @ 2.50% of the total RWA will be maintained in the form of CET1 in a phased manner from 2016 to 2019.

Tier I capital of the Bank includes funds deposited with Bangladesh Bank, actuarial gain/(loss) and retained earnings. Tier 1 capital is also called 'Core Capital' of the Bank. According to BRPD letter ref no.BRPD (BFIS)661/14B(P)/2015-18014 dated 24 December 2015, 5% of deferred tax recognised on specific provision shall be allowable as CET 1 capital whilst all other deferred tax assets created on other items shall be deducted from the retained earnings when calculating the capital adequacy ratio.

Tier II capital consists of general provision and revaluation reserve for Held to Maturity (HTM) and Held for Trading (HFT) securities. According to BRPD circular no. 05 (31 May 2016) the full general provision maintained against unclassified loans and advances (except Fast Track Electricity Project LC) will be considered as Tier II capital. Revaluation reserve for securities shown as Tier II capital as on 31 December 2014 will be nullified in a phased manner at the rate of 20% starting from 2015 and will be fully adjusted by 2020.

Quantitative disclosures:

The details of capital structure are provided as under:	2018 BDT	2017 BDT
Common Equity Tier I		
Fund deposited with Bangladesh Bank	3,099,690,272	3,072,581,767
Retained earnings	27,658,950,379	26,335,857,369
Actuarial gain/(loss)	(53,707,814)	(119,289,763)
Less: Regulatory adjustment for deferred tax assets as per the Bangladesh Bank guideline	(249,318,905)	(307,888,151)
	30,455,613,932	**28,981,261,222**
Additional Tier I	-	-
	-	-
Total Tier I	**30,455,613,932**	**28,981,261,222**
Tier II		
General provision	2,829,733,135	2,503,599,728
Revaluation reserve for securities	16,989,823	33,979,646
	2,846,722,958	**2,537,579,374**
Total capital	**33,302,336,890**	**31,518,840,596**

4 Capital adequacy

Qualitative disclosures:

The Bank has adopted the Standardised Approach for computation of the capital charge for credit risk and market risk, and the Basic Indicator Approach for operational risk. Assessment of capital adequacy is carried out in conjunction with the capital adequacy reporting to the Bangladesh Bank.

The Bank has a capital adequacy ratio of 26.72% as against the minimum regulatory requirement of 11.875% including capital conservation buffer. Tier I capital adequacy ratio is 24.44% against the minimum regulatory requirement of 6%. The Bank's policy is to manage and maintain its capital with the objective of maintaining a strong capital ratio. The Bank maintains capital levels that are sufficient to absorb all material risks. The Bank also ensures that the capital levels comply with all regulatory requirements, satisfy external rating agencies and other stakeholders including depositors. The whole objective of the capital management process in the Bank is to ensure that the Bank remains adequately capitalised at all times.

The Bank has in place a capital adequacy framework by which the Bank's annual budget projections and the capital required to achieve the business objectives are linked in a cohesive way. Capital requirements are assessed for credit, market and operational risks. The Bank's capital adequacy ratio is periodically assessed and reviewed by the ALCO and reported to head office. The composition of capital in terms of Tier I and II are also analysed to ensure capital stability and to reduce volatility in the capital structure. The Bank has a profit remittance policy to ensure that the Bank has enough capital to comply with the regulatory requirement. The Bank's capital plan also ensures that adequate levels of capital are held considering the planned organic growth of the business.

Quantitative disclosures:

	2018 BDT Risk Weighted Assets	2017 BDT Risk Weighted Assets
On balance sheet items	59,518,679,338	50,288,164,090
Off balance sheet items	47,172,763,239	34,234,968,238
Total credit risk	106,691,442,577	84,523,132,328
Market risk	2,153,824,676	1,475,194,880
Operational risk	15,775,281,690	17,826,620,867
Total risk weighted assets	**124,620,548,943**	**103,824,948,075**

Detail of capital adequacy

	2018	2017
Capital requirement for credit risk	12,669,608,806	9,508,852,387
Capital requirement for market risk	255,766,680	165,959,424
Capital requirement for operational risk	1,873,314,701	2,005,494,848
Total required capital	**14,798,690,187**	**11,680,306,659**
Common Equity Tier I capital	30,455,613,932	28,981,261,221
Total Tier I capital	30,455,613,932	28,981,261,221
Total Tier II capital	2,846,722,958	2,537,579,374
Total regulatory capital	**33,302,336,890**	**31,518,840,595**
Surplus	**18,503,646,703**	**19,838,533,936**
% of Capital adequacy required		
Common Equity Tier I	6.375%	5.750%
Tier I	6.000%	6.000%
Total	11.875%	11.250%
% of Capital adequacy maintained		
Common Equity Tier I	24.44%	27.91%
Tier I	24.44%	27.91%
Total	26.72%	30.36%

5 Credit Risk

Qualitative disclosures:

Credit risk is the risk of financial loss if a customer or counterparty fails to meet a payment obligation under a contract. It arises principally from direct lending, trade finance and leasing business, but also from off balance sheet products such as guarantees and credit derivatives, and from the holdings of debt securities. HSBC Bangladesh has standards, policies and procedures dedicated to controlling and monitoring risk from all such activities. Among the risks the Bank engages in, credit risk generates the largest regulatory capital requirement.

The aims of credit risk management, underpinning sustainably profitable business, are principally

- to maintain a strong culture of responsible lending, supported by a robust risk policy and control framework;
- to both partner and challenge business originators effectively in defining and implementing risk appetite, and its re-evaluation under actual and scenario conditions; and
- to ensure independent, expert scrutiny and approval of credit risks, their costs and their mitigation.

The standardised approach is applied for risk weighting of exposure as per directive of Bangladesh Bank. It requires banks to use risk assessments prepared by External Credit Assessment Institutions (ECAIs) to determine the risk weightings applied to rated counterparties. The Bank has applied some customer ratings based on their entity rating as assigned by the approved ECAIs of Bangladesh Bank.

It is HSBC's policy to establish that loans are within the customer's capacity to repay, rather than to rely excessively on security. Depending on the customer's standing and the type of product, facilities may be unsecured. Nevertheless, collateral can be an important mitigant of credit risk.

The Bank has guidelines on the acceptability of specific classes of collateral or credit risk mitigation, and determines suitable valuation parameters. Such parameters are expected to be conservative, reviewed regularly and supported by empirical evidence. Security structures and legal covenants are required to be subject to regular review to ensure that they continue to fulfill their intended purpose and remain in line with local market practice. The principal collateral types are as follows:

- Cash collateral
- In the personal sector, mortgages over residential properties
- In the commercial and industrial sector, charges over business assets such as premises, stock and debtors, plan and machineries

Special attention is given to problem loans and appropriate action is initiated to protect the Bank's position on a timely basis and to ensure that loan impairment methodologies result in losses being recognised when they are incurred. The objective of credit risk management is to minimise the probable losses and maintaining credit risk exposure within acceptable parameters.

HSBC has historically sought to maintain a conservative, yet constructive and competitive credit risk culture. This has served the Group well, through successive economic cycles and remains valid today. This culture is determined and underpinned by the disciplined credit risk control environment which the Group has put in place to govern and manage credit risk, and which is embodied in the formal policies and procedures adopted by HSBC Bangladesh. These are articulated through Group credit policies supplemented by regional and local area lending guidelines, backed up by the Bangladesh Bank's "Managing Core Risks in Banking - Credit Risk Management - Industry Best Practices" and "Guidelines on Credit Risk Management (CRM) for Banks". Formal policies and procedures cover all areas of credit lending and monitoring processes including:

- The Group Credit Risk Policy Framework
- Risk appetite and evaluation of facilities
- Key lending constraints and higher-risk sectors
- Risk rating systems
- Facility structures
- Lending to banks, non-banks and sovereigns
- Personal lending
- Corporate and commercial lending
- Portfolio management and stress testing
- Monitoring, control and the management of problem exposures
- Impairments and allowances

At the heart of these processes is a robust framework of accountability. HSBC operates a system of personal credit authorities, not credit committee structures. However, the Bank has set up a Risk Management Meeting (RMM) comprising all the members of the Asset Liability Committee (ALCO) and other risk related function heads to manage various risks within the Bank including credit risk. Relationship Managers are held accountable for both the profitability and growth of their loan portfolios as well as the losses that may arise within them.

The Bank also has established a separate Risk Department which looks after the loan review mechanism and also helps in ensuring credit compliance with the post-sanction processes/ procedures laid down by the Bank from time to time. This involves taking up independent account-specific reviews of individual credit exposures as per the approved lending guideline. The Risk department also monitors various credit concentration limits. The Bank has in place a risk grading system for analysing the risk associated with credit. The parameters for risk grading customers include financial condition and performance, quality of disclosures and management, facility structure, collateral and country risk assessment where necessary. Maximum funded counterparty/group exposures are limited to 15% of the Bank's capital base as stipulated by Bangladesh Bank. Where a higher limit is required for projects of national importance, prior approval of Bangladesh Bank is obtained.

Past dues and impaired exposures are defined in accordance with the relevant Bangladesh Bank regulations. Specific and general provisions are computed periodically in accordance with Bangladesh Bank regulations.

Credit risk mitigation

The Bank has adopted the simple approach for credit risk mitigation under the standardised approach where only cash collaterals are considered against the exposures to calculate the net exposure with applicable haircut.

Specific provision

The Bank follows Bangladesh Bank guidelines regarding loan classifications, provisioning and any other issues related to Non Performing Loan (NPL). The Bank's internal credit guidelines also give direction on the management of NPLs, the procedure for reviewing loan provisioning, debt write off, facility grading, reporting requirements and interest recognition. However, the Bank's guidelines will not supersede local regulations. Thus, while dealing with NPLs, the Bank's decision is always compliant with local rules and regulations as well as Group guidelines which are more conservative than local regulations.

Throughout the year the Bank reviews loans and advances to assess whether objective evidence has arisen of impairment of a loan or portfolio that warrants a change in the classification of loans and advances which may result in a change in the provision required in accordance with BRPD circular no.14 (23 September 2012) as amended by BRPD circular no. 19 (27 December 2012). The guidance in the circulars follows a formulaic approach whereby specified rates are applied to the various categories of loans as defined in the circulars. The provisioning rates are as follows:

Specific provision on loans and advances

Specific provision on substandard loans and advances/investments other than agricultural loans	20%
Specific provision on doubtful loans and advances/investment other than agricultural loans	50%
Specific provision on substandard and doubtful agricultural loans	5%
Specific provision on bad / loss and advances/investments	100%

BRPD circular no.14 (23 September 2012) as amended by BRPD circular no. 19 (27 December 2012) also provides scope for further provisioning based on qualitative judgments. In these circumstances, impairment losses are calculated on individual loans considered individually significant based on which specific provisions are raised. If the specific provisions assessed under the qualitative methodology are higher than the specific provisions assessed under the formulaic approach above, the higher of the two is recognised in liabilities under "Provisions for loans and advances" with any movement in the provision charged/released in the profit and loss account.

Quantitative disclosures:

Gross Credit Risk Exposure	**2018 BDT**	**2017 BDT**
Claims on sovereigns and central banks	45,752,716,160	27,976,630,606
Claims on banks	4,804,460,292	3,803,560,788
Investments	7,915,203,878	10,555,016,889
Claims on corporate	76,309,843,731	60,113,556,318
Claims on consumer	5,598,280,667	6,858,313,277
Fixed assets	292,843,266	333,843,488
All other assets	5,897,354,667	9,805,824,640
Total on-balance sheet items	146,570,702,660	119,446,746,006
Off-balance sheet items (after considering the credit conversion factor)	67,874,238,716	46,397,855,994
Total	**214,444,941,376**	**165,844,602,000**

Geographical distribution of credit exposures

2018	Dhaka	Chattogram	Total BDT
Claims on sovereigns and central banks	44,872,775,722	879,940,437	45,752,716,160
Claims on banks	4,804,460,292	-	4,804,460,292
Investments	7,913,400,978	1,802,900	7,915,203,878
Claims on corporate	65,969,684,816	10,340,158,915	76,309,843,731
Claims on consumer	4,724,947,636	873,333,032	5,598,280,667
Fixed assets	225,104,928	67,738,337	292,843,266
All other assets	5,861,966,568	35,388,099	5,897,354,667
Total on-balance sheet items	134,372,340,940	12,198,361,721	146,570,702,660
Off-balance sheet items	63,364,761,148	4,509,477,568	67,874,238,716
Total	**197,737,102,088**	**16,707,839,289**	**214,444,941,376**

2017	Dhaka	Chattogram	Total BDT
Claims on sovereigns and central banks	26,980,987,114	995,643,492	27,976,630,606
Claims on banks	3,803,560,788	-	3,803,560,788
Investments	10,553,460,989	1,555,900	10,555,016,889
Claims on corporate	50,689,868,210	9,423,688,108	60,113,556,318
Claims on consumer	5,590,355,721	1,267,957,557	6,858,313,278
Fixed assets	251,706,030	82,137,458	333,843,488
All other assets	9,754,082,891	51,741,748	9,805,824,639
Total on-balance sheet items	107,624,021,743	11,822,724,263	119,446,746,006
Off-balance sheet items	42,852,547,270	3,545,308,724	46,397,855,994
Total	**150,476,569,013**	**15,368,032,987**	**165,844,602,000**

Industry distribution of exposures

2018	Banks and FIs	Manufacturing	Industry	Retail	Others	Total BDT
Claims on sovereigns and central banks	45,752,716,160	-	-	-	-	45,752,716,160
Claims on banks	4,804,460,292	-	-	-	-	4,804,460,292
Investments	-	-	-	-	7,915,203,878	7,915,203,878
Claims on corporate	-	37,578,118,257	25,641,660,899	-	13,090,064,576	76,309,843,731
Claims on consumer	-	-	-	4,449,619,007	1,148,661,660	5,598,280,667
Fixed assets	-	-	-	-	292,843,266	292,843,266
All other assets	-	-	-	-	5,897,354,667	5,897,354,667
Total on-balance sheet items	50,557,176,451	37,578,118,257	25,641,660,899	4,449,619,007	28,344,128,046	146,570,702,660
Off-balance sheet items	22,295,126,694	-	-	-	45,579,112,022	67,874,238,716
Total	**72,852,303,145**	**37,578,118,257**	**25,641,660,899**	**4,449,619,007**	**73,923,240,068**	**214,444,941,376**

2017	Banks and FIs	Manufacturing	Industry	Retail	Others	Total BDT
Claims on sovereigns and central banks	27,976,630,606	-	-	-	-	27,976,630,606
Claims on banks	3,803,560,788	-	-	-	-	3,803,560,788
Investments	-	-	-	-	10,555,016,889	10,555,016,889
Claims on corporate	-	31,327,362,706	21,058,323,994	-	7,727,869,618	60,113,556,318
Claims on consumer	-	-	-	6,395,725,753	462,587,524	6,858,313,277
Fixed assets	-	-	-	-	333,843,488	333,843,488
All other assets	-	-	-	-	9,805,824,640	9,805,824,640
Total on-balance sheet items	31,780,191,394	31,327,362,706	21,058,323,994	6,395,725,753	28,885,142,159	119,446,746,006
Off-balance sheet items	15,008,078,441	-	-	-	31,389,777,553	46,397,855,994
Total	**46,788,269,835**	**31,327,362,706**	**21,058,323,994**	**6,395,725,753**	**60,274,919,712**	**165,844,602,000**

Maturity breakdown of credit exposures

2018	Within 1 month	Within 1 to 3 months	Within 3 to 12 months	Within 1 to 5 years	Over 5 years	Total BDT
Claims on sovereigns and central banks	39,749,639,332	-	-	-	6,003,076,828	45,752,716,160
Claims on banks	4,804,460,292	-	-	-	-	4,804,460,292
Investments	1,507,862,515	550,716,344	5,856,625,018	-	-	7,915,203,878
Claims on corporate	16,029,119,774	20,940,138,384	28,650,689,387	10,080,685,202	609,210,984	76,309,843,731
Claims on consumer	21,104,351	72,896,255	200,222,569	3,525,838,468	1,778,219,024	5,598,280,667
Fixed assets	152,684	3,273,548	24,320,688	211,964,043	53,132,303	292,843,266
All other assets	1,964,747,220	2,281,180,066	350,465,066	834,862,841	466,099,473	5,897,354,666
Total on-balance sheet items	64,077,086,168	23,848,204,598	35,082,322,729	14,653,350,554	8,909,738,612	146,570,702,660
Off-balance sheet items	8,222,753,182	14,642,968,163	31,408,887,543	13,599,629,828	-	67,874,238,716
Total	**72,299,839,350**	**38,491,172,761**	**66,491,210,272**	**28,252,980,382**	**8,909,738,612**	**214,444,941,376**

2017	Within 1 month	Within 1 to 3 months	Within 3 to 12 months	Within 1 to 5 years	Over 5 years	Total BDT
Claims on sovereigns and central banks	25,004,761,483	-	-	-	2,971,869,123	27,976,630,606
Claims on banks	3,803,560,788	-	-	-	-	3,803,560,788
Investments	1,534,562,621	2,107,491,428	4,815,712,892	2,097,249,949	-	10,555,016,890
Claims on corporate	17,685,931,431	13,789,812,234	21,873,470,008	6,452,284,001	312,058,644	60,113,556,318
Claims on consumer	570,300,114	80,034,270	163,288,215	4,182,076,422	1,862,614,256	6,858,313,277
Fixed assets	8,074,045	496,977	12,863,909	210,399,406	102,009,151	333,843,488
All other assets	7,372,653,151	1,389,019,096	426,544,968	612,285,558	5,321,866	9,805,824,639
Total on-balance sheet items	55,979,843,633	17,366,854,005	27,291,879,992	13,554,295,336	5,253,873,040	119,446,746,006
Off-balance sheet items	7,289,163,330	13,149,973,793	14,221,578,090	11,737,140,781	-	46,397,855,994
Total	**63,269,006,963**	**30,516,827,798**	**41,513,458,082**	**25,291,436,117**	**5,253,873,040**	**165,844,602,000**

Gross Non Performing Assets (NPAs)

	2018 BDT	2017 BDT
Non Performing Assets (NPAs) to outstanding loans and advances	1,475,858,628	1,573,244,596
Movement of NPAs		
Opening Balance	1,573,244,596	1,546,816,754
Written off during the period	(229,811,807)	(184,493,595)
Recoveries during the period	(81,515,249)	(94,150,050)
Addition during the period	213,941,087	305,071,487
Closing Balance	**1,475,858,628**	**1,573,244,596**
Movement of specific provision for NPAs		
Opening Balance	674,300,505	678,083,447
Written off (net off recovery) during the period	(60,155,650)	(60,551,886)
Recoveries during the period	(61,797,309)	(160,030,590)
Provision made during the period	167,736,459	216,799,534
Closing Balance	**720,084,005**	**674,300,505**

6 Equities: Disclosures for banking book positions

The bank does not hold trading position in equities.

7 Interest rate risk in the banking books

Discussed in the next section under Market risk.

8 Market risk

Qualitative disclosures:

Market risk is the risk to the Bank's earnings and capital due to changes in the market level of interest rates or prices of securities, foreign exchange and equities, as well as the volatilities of those changes.

The Bank uses the standardised (market risk) approach to calculate market risk for trading book exposures. The trading book consists of positions in financial instruments held with trading intent or in order to hedge other elements of the trading book. A capital charge will be applicable for financial instruments which are free from any restrictive covenants on tradability, or able to be hedged completely. Generally, investments in 'Held for Trading' portfolios are focal parts of the trading book.

Capital charge means an amount of regulatory capital which the Bank is required to hold for an exposure to a relevant risk which, if multiplied by 10, becomes the risk-weighted amount of that exposure for that risk.

The Bank has a comprehensive treasury risk policy which inter alia covers assessment, monitoring and management of all the above market risks. The Bank has defined various internal limits to monitor market risk and is computing the capital requirement as per the standardised approach of Basel III.

Details of various market risks faced by the Bank are set out below:

Interest rate exposures

The Bank adopts the maturity method in measuring interest rate risk in respect of securities in the trading book. The capital charge for the entire market risk exposure is computed under the standardised approach using the maturity method and in accordance with guidelines issued by Bangladesh Bank.

Interest rate exposures in the banking book

Interest rate risk is the risk where changes in market interest rates might adversely affect a bank's financial condition. The immediate impact of changes in interest rates is on the Net Interest Income (NII). A long term impact of changing interest rates is on the Bank's net worth since the economic value of a Bank's assets, liabilities and off-balance sheet positions are affected by a variation in market interest rates. The responsibility of interest rate risk management rests with the Bank's Asset and Liability Management Committee (ALCO). The Bank periodically computes the interest rate risk on the banking book that arises due to re-pricing mismatches in interest rate sensitive assets and liabilities. For the purpose of monitoring such interest rate risk, the Bank has in place a system that tracks the re-pricing mismatches in interest bearing assets and liabilities. For computation of the interest rate mismatches the guidelines of Bangladesh Bank are followed.

Foreign exchange risk

Foreign exchange risk is defined as the risk that a bank may suffer losses as a result of adverse exchange rate movements during a period in which it has an open position, either spot or forward, or a combination of the two, in an individual foreign currency. The responsibility of management of foreign exchange risk rests with the Global Markets department of the Bank. The Bank has set up internal limits to monitor foreign exchange open positions. Foreign exchange risk is computed on the sum of net short positions or net long positions, whichever is higher of the foreign currency positions held by the Bank.

Equity position risk

The Bank does not hold a trading position in equities.

Quantitative disclosures:

The capital charge for various components of market risk is presented below:

The capital requirement for:

	2018 BDT	2017 BDT
Interest rate risk	35,230,937	104,554,312
Equity position risk	-	-
Foreign exchange risk	180,151,531	42,965,176
Commodity risk	-	-
	215,382,468	**147,519,488**

9 Operational risk

Qualitative disclosures:

Operational risk is the risk of loss arising from inadequate or failed internal processes, people and systems or external events, including legal risk. It is inherent in every business organisation and covers a wide spectrum of issues. The Group manages this risk through a control based environment in which processes are documented, authorisation is independent and transactions are reconciled and monitored. This is supported by an independent programme of periodic reviews undertaken by internal audit and control testing and by monitoring external operational risk events, which ensure that the Group stays in line with industry best practice and takes account of lessons learned from publicised operational failures within the financial services industry.

The Group has codified its operational risk management process by issuing a high level standard, supplemented by more detailed formal guidance. This explains how the Group manages operational risk by identifying, assessing, monitoring, controlling and mitigating the risk, rectifying operational risk events, and implementing any additional procedures required for compliance with local regulatory requirements. The standard covers the following:

- Operational risk management responsibility is assigned to senior management within the business operation;
- Information systems are used to record the identification and assessment of operational risks and to generate appropriate, regular management reporting;
- Assessments are undertaken of the operational risks facing each business and the risks inherent in its processes, activities and products. Risk assessment incorporates a regular review of identified risks to monitor significant changes;
- Operational risk loss data is collected and reported to senior management. Aggregate operational risk losses are recorded and details of incidents above a materiality threshold are reported to the Group's Audit Committee; and
- Risk mitigation, including insurance, is considered where this is cost-effective.

The Group maintains and tests contingency facilities to support operations in the event of disasters. Additional reviews and tests are conducted in the event that any HSBC office is affected by a business disruption event, to incorporate lessons learned in the operational recovery from those circumstances. Plans have been prepared for the continued operation of the Group's business, with reduced staffing levels.

In line with the instructions from the Bangladesh Bank, the Bank uses the basic indicator approach to calculate its operational risk.

Quantitative disclosures:

	2018 BDT	2017 BDT
Capital charge for operational risk	1,577,528,169	1,782,662,087

10 Liquidity Ratio

Qualitative disclosures:

Liquidity Risk is the risk that the bank does not have sufficient financial resources to meet its obligations as they fall due or will have to do so at excessive cost. The risk arises from mismatch in the timing of cash flows.

The objective of liquidity framework is to allow the Bank to withstand very severe stresses. It is designed to be adaptable to change the business modes, markets and regulators. The liquidity risk management frameworks requires:

- liquidity to managed by Bank on stand-alone basis with no reliance on the Bangladesh Bank;
- to comply with all regulatory limits;
- to maintain positive stressed cash flow;
- monitoring the contingent funding commitments;

- monitoring the structural term mismatch between maturing assets and liabilities;
- maintenance of robust and practical liquidity contingency plan;
- maintain diverse sources of funding and adequate back up lines

Liquidity management of the Bank is centered on the Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR) based on BASEL III. The Bank has Asset Liability Management (ALM) desk to manage this risk with active monitoring and management from Global Markets Department.

The Bank has adopted Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR) for liquidity risk management. LCR ensures that banks maintain enough high quality unencumbered liquid assets to meet its liquidity needs for 30 calendar time-line whereas NSFR ensures availability of stable funding is greater than required funding over 1 year period.

Bank has Asset Liability Management Committee (ALCO) to monitor the liquidity risk on a monthly basis. Based on the detail recommendation from ALM desk, ALCO take appropriate action to manage the liquidity risk. To have more conservative approach towards liquidity risk measurement, the Bank has set internal LCR and NSFR limits which are more stringent and set higher than the regulatory limit of 100%. These ratios are regularly monitored at ALCO. Also Bank has internal risk control framework which outlines clear and consistent policies and principles for liquidity risk management.

Quantitative disclosures:

	2018 BDT	2017 BDT
Liquidity coverage ratio (%)	119.92%	111.13%
Net Stable Funding Ratio (%)	109.15%	111.96%
Stock of High quality liquid assets	63,630,750,251	48,878,111,009
Total net cash outflows over the next 30 calendar days	53,062,849,333	43,981,628,964
Available amount of stable funding	133,411,158,384	110,932,037,593
Required amount of stable funding	122,228,170,674	99,081,583,983

11 Leverage Ratio

Qualitative disclosures:

Leverage ratio is the ratio of tier 1 capital to total on- and off-balance sheet exposures. The leverage ratio was introduced into the Basel III framework as a non-risk based backstop limit, to supplement risk-based capital requirements.

In order to avoid building-up excessive on- and off-balance sheet leverage in the banking system, a simple, transparent, non-risk based leverage ratio has been introduced by the Bangladesh Bank. The leverage ratio is calibrated to act as a credible supplementary measure to the risk based capital requirements. The leverage ratio is intended to achieve the following objectives:

- constrain the build-up of leverage in the banking sector which can damage the broader financial system and the economy; and
- reinforce the risk based requirements with an easy to understand and a non-risk based measure.

The Bank has calculated the regulatory leverage ratio as per the guideline of Basel III. The numerator, capital measure is calculated using the new definition of Tier I capital applicable from 01 January 2015. The denominator, exposure measure, is calculated on the basis of the Basel III leverage ratio framework as adopted by the Bangladesh Bank. The exposure measure generally follows the accounting value, adjusted as follows:

- on-balance sheet, non derivative exposures are included in the exposure measure net of specific provision;
- physical or financial collateral is not considered to reduce on-balance sheet exposure;
- loans are not netted with deposits;
- off-balance sheet items are converted into credit exposure equivalents through the use of credit conversion factors (CCFs). Depending on the risk category of the exposure a CCF of 20%, 50% or 100% is applied. Commitments that are unconditionally cancellable at any time by the bank without

prior notice, a CCF of 10% is applied;

- item deducted from Tier I capital such as deferred tax assets.

Quantitative disclosures:

	2018 BDT	2017 BDT
Leverage ratio	12.05%	14.51%
On balance sheet exposure	166,933,210,109	140,134,671,763
Off balance sheet exposure	85,994,228,492	59,916,994,610
Total exposure	252,927,438,601	200,051,666,373

12 Remuneration

Qualitative disclosures:

The Bank has a Group specified remuneration policy which is designed to reward competitively the achievement of long-term sustainable performance and attract and motivate the very best people who are committed to maintaining a long-term career with HSBC and performing their role in the long-term interests of shareholders. The Group Remuneration Committee oversees the remuneration policy and are responsible for setting the overarching principles, parameters and governance framework of the remuneration policy. All members of the Committee are independent non-executive Directors of HSBC Holdings plc. The Committee periodically reviews the adequacy and effectiveness of the Group's remuneration policy and ensures that the policy meets the commercial requirement to remain competitive, is affordable, allows flexibility in response to prevailing circumstances and is consistent with effective risk management.

HSBC's reward strategy aims to reward success and be properly aligned with Bank's risk framework and related outcomes. In order to ensure alignment between remuneration and the Bank's business strategy, individual remuneration is determined through assessment of performance delivered against both annual and long term objectives summarised in performance scorecards as well as adherence to the HSBC Values of being 'open, connected and dependable' and acting with 'courageous integrity'. Altogether performance is judged, not only on what is achieved over the short and long term, but also on how it is achieved, as the later contributes to the sustainability of the organisation.

HSBC's reward package consists of the following key elements:

Fixed Pay:

The purpose of the fixed pay is to attract and retain employees by paying market competitive pay for the role, skills and experience required for the business. This includes salary, fixed pay allowance, and other cash allowances in accordance with local market practices. These payments are fixed and do not vary with performance.

Benefits:

HSBC provides benefits in accordance with local and international market practice. This includes but is not limited to the provision of pensions, medical insurance, life insurance and relocation allowances etc.

Annual Incentive:

HSBC provides annual incentive to drive and reward performance based on annual financial and non-financial measures consistent with the medium to long-term strategy, shareholder interests and adherence to HSBC values. Awards can be in the form of cash and shares. A portion of the annual incentive award is deferred and vests over a period of 3 years. The Bank pays the incentive in the form of cash.

Under the remuneration framework remuneration decisions are made based on a combination of business results, performance against objectives set out in performance scorecards, general individual performance of the role and adherence to the HSBC values, business principles, Group risk-related policies and procedures and Global Standards.

Key features of HSBC's remuneration framework include:

- assessment of performance with reference to clear and relevant objectives set within a performance scorecard framework;

- a focus on total compensation (fixed plus variable pay) with variable pay (namely annual incentive and the value of long term incentives) differentiated by performance and adherence to HSBC values;
- the use of discretion to assess the extent to which performance has been achieved; and
- deferral of a significant proportion of variable pay into HSBC shares to tie recipients to the future performance of the Group and align the relationship between risk and reward.

Within this framework, risk alignment of our remuneration structure is achieved through the following measures:

- Risk and compliance is a critical part of the assessment process in determining the performance of all employees, especially senior executives and identified staff and material risk takers. All employees are required to have risk measures in their performance scorecards, which ensure that their individual remuneration has been appropriately assessed with regard to risk.
- Adherence to HSBC values is a pre-requisite for any employee to be considered for variable pay. HSBC values are key to the running of a sound, sustainable bank. Employees have a separate HSBC values rating which directly influences their overall performance rating considered by the Committee for their variable pay determinations.
- For our most senior employees, the greater part of their reward is deferred and thereby subject to malus, which allows the awards to be reduced or cancelled if warranted.
- The Group also carries out regular reviews to assess instances of non-compliance with risk procedures and expected behaviour. Instances of non-compliance are escalated for consideration in variable pay decisions, including adjustments and malus of unvested awards granted in prior years. For identified staff and Material Risk Takers (MRTs), the Committee has oversight of such decisions.
- All variable pay awards made to identified staff and material risk takers for the performance year in which they have been identified as MRTs are also subject to the Group Claw back Policy in accordance with the requirements in the Prudential Regulation Authority's Remuneration Code.

Quantitative disclosures:

	2018 BDT	2017 BDT
Number of meetings held by the main body overseeing remuneration during the financial year	n/a	n/a
Remuneration paid to the main body overseeing remuneration during the financial year	n/a	n/a
Number of employees having received a variable remuneration award during the financial year	763	770
Guaranteed bonuses awarded during the financial year:		
Number of employee	860	847
Total amount of guaranteed bonuses	80,668,542	76,045,093
Sign-on awards made during the financial year:		
Number of employee	-	-
Total amount of sign-on awards	-	-
Severance payments made during the financial year:		
Number of employee	7	1
Total amount of severance payments	35,867,138	8,827,049
Total amount of outstanding deferred remuneration (in cash)	6,640,832	11,039,004
Total amount of deferred remuneration paidout in the financial year	5,913,855	4,781,294
Breakdown of amount of remuneration awards for the financial year:		
Fixed and variable	2,081,067,335	2,190,273,206
Variable pay		
Deferred	7,414,662	7,007,823
Non-deferred	373,521,837	375,162,565
	380,936,499	382,170,388