

HSBC, Bangladesh

Disclosures on risk based capital
under Pillar - III of Basel III
for the year ended 31 December 2020



The Hongkong and Shanghai Banking Corporation Limited, Bangladesh Branches

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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 12.50% (including capital conservation buffer @2.50%) 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 aligned with regulatory capital structure. Tier I capital is 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) of 2.50% of the total RWA has to be maintained from 2020 and onwards.

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. 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.

Quantitative disclosures:

The details of capital structure are provided as under:

	2020	2019
	BDT	BDT
Common Equity Tier I		
Fund deposited with Bangladesh Bank	3,135,747,494	3,135,747,494
Retained earnings	38,929,347,049	34,925,113,033
Actuarial gain / (loss)	(433,284,241)	(7,183,986)
Less: Regulatory adjustment for deferred tax assets as per the Bangladesh Bank guideline	(686,210,828)	(294,685,170)
	40,945,599,474	37,758,991,371
Additional Tier I	-	-
	-	-
Total Tier I	40,945,599,474	37,758,991,371
Tier II		
General provision	3,559,660,068	3,399,243,410
Revaluation reserve for securities	-	-
	3,559,660,068	3,399,243,410
Total capital	44,505,259,542	41,158,234,781

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 23.21% as against the minimum regulatory requirement of 12.50% including capital conservation buffer. Tier I capital adequacy ratio is 21.35% 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:

Position of various risk weighted assets are presented below:

	2020	2019
	BDT	BDT
	Risk Weighted Assets	Risk Weighted Assets
On balance sheet items	147,845,592,995	205,656,181,467
Off balance sheet items	21,618,389,247	24,968,198,532
Total credit risk	169,463,982,242	230,624,379,999
Market risk	753,192,637	4,141,146,946
Operational risk	21,555,330,923	20,447,836,467
Total risk weighted assets	191,772,505,802	255,213,363,412

Detail of capital adequacy

	2020 BDT	2019 BDT
Capital requirement for credit risk	21,182,997,780	28,828,047,500
Capital requirement for market risk	94,149,080	517,643,368
Capital requirement for operational risk	2,694,416,365	2,555,979,558
Total required capital	23,971,563,225	31,901,670,426
Common Equity Tier I capital	40,945,599,474	37,758,991,371
Total Tier I capital	40,945,599,474	37,758,991,371
Total Tier II capital	3,559,660,068	3,399,243,410
Total regulatory capital	44,505,259,542	41,158,234,781
Surplus	20,533,696,317	9,256,564,355
% of Capital adequacy required		
Common Equity Tier I	7.000%	7.000%
Tier I	6.000%	6.000%
Total	12.500%	12.500%
% of Capital adequacy maintained		
Common Equity Tier I	21.35%	14.80%
Tier I	21.35%	14.80%
Tier II	1.86%	1.33%
Capital Conservation Buffer	15.35%	8.80%
Total	23.21%	16.13%

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
- to ensure independent, expert scrutiny and approval of credit risks, their costs and their mitigation.

HSBC has historically been maintaining 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 in line with Bangladesh Bank and other local regulations. Formal policies and procedures cover all areas of credit lending and monitoring processes including, but not limited to:

- 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. Business segments are responsible for both the profitability and growth of their loan portfolios as well as the losses that may arise within them. Credit Risk Management function of the Bank is responsible for credit risk assessment and approval process. In addition, as part of overall risk governance framework, the Bank has in place a Risk Management Meeting (RMM) forum chaired by the Chief Risk Officer in presence of the Chief Executive Officer and all Business and Function Heads within the Bank.

The Bank also has relevant Departments to look after the loan review mechanism and also to ensure 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 and also monitoring various credit concentration limits as per the lending guideline. In line with Bangladesh Bank's guideline, the Bank has credit risk grading system in place for analysing the risk associated with credit.

The standardised approach is applied for risk weighting of exposure as per directive of Bangladesh Bank. It requires banks to use credit rating assigned by External Credit Assessment Institutions (ECAIs), where available, to determine the risk weightings applied to rated counterparties.

The Bank has been maintaining credit risk mitigation under the standardised approach. It is HSBC's policy to establish that loans are within the customer's capacity to repay which is also supported by collaterals as an important mitigation of credit risk wherever necessary. The Bank has guidelines on the acceptability of different types of collateral or credit risk mitigation, and determines suitable valuation parameters. Such parameters are being reviewed regularly and supported by empirical evidence.

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

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.

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. Thus, while dealing with NPLs, the Bank's decision is always compliant with local rules and regulations as well as Group guidelines.

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. 56 (10 December 2020), BRPD circular No. 52 (20 October 2020), BRPD circular No. 17 (28 September 2020), BRPD Circular No. 16 (21 July 2020), BRPD circular No. 13 (15 June 2020), BRPD circular No. 04 (19 March 2020), BRPD circular No. 07 (19 March 2020), BRPD circular No. 24 (17 November 2019), BRPD circular No. 06 (19 May 2019), BRPD circular No. 04 (16 May 2019), BRPD circular No. 03 (21 April 2019), BRPD circular No. 01 (20 February 2018), BRPD circular No.15 (27 September 2017), BRPD circular No.16 (18 November 2014), BRPD circular No.14 (23 September 2012), BRPD circular No. 19 (27 December 2012) and BRPD circular No. 05 (29 May 2013). 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

	2020 BDT	2019 BDT
Claims on sovereigns and central banks	36,706,487,911	30,083,846,873
Claims on banks	11,192,997,458	19,595,350,374
Investments	39,279,285,462	16,278,988,469
Claims on corporate	226,709,255,603	216,045,288,281
Claims on consumer	4,338,258,826	4,578,642,563
Fixed assets	322,474,322	266,899,913
All other assets	2,880,155,852	4,624,835,382
Total on-balance sheet items	<u>321,428,915,434</u>	<u>291,473,851,855</u>
Off-balance sheet items (after considering the credit conversion factor)	<u>32,712,834,470</u>	<u>32,493,460,821</u>
Total	<u>354,141,749,904</u>	<u>323,967,312,676</u>

Geographical distribution of credit exposures

2020	Dhaka	Chattogram	Total BDT
Claims on sovereigns and central banks	34,492,107,428	2,214,380,483	36,706,487,911
Claims on banks	11,192,997,458	-	11,192,997,458
Investments	39,278,360,462	925,000	39,279,285,462
Claims on corporate	198,966,638,999	27,742,616,604	226,709,255,603
Claims on consumer	3,754,279,585	583,979,241	4,338,258,826
Fixed assets	284,254,926	38,219,396	322,474,322
All other assets	2,803,911,943	76,243,909	2,880,155,852
Total on-balance sheet items	<u>290,772,550,801</u>	<u>30,656,364,633</u>	<u>321,428,915,434</u>
Off-balance sheet items	<u>30,950,306,694</u>	<u>1,762,527,776</u>	<u>32,712,834,470</u>
Total	<u>321,722,857,495</u>	<u>32,418,892,409</u>	<u>354,141,749,904</u>

2019	Dhaka	Chattogram	Total BDT
Claims on sovereigns and central banks	29,427,028,989	656,817,884	30,083,846,873
Claims on banks	19,595,350,374	-	19,595,350,374
Investments	16,278,095,469	893,000	16,278,988,469
Claims on corporate	205,948,452,926	10,096,835,354	216,045,288,281
Claims on consumer	3,787,031,909	791,610,654	4,578,642,563
Fixed assets	213,899,632	53,000,281	266,899,913
All other assets	4,591,510,393	33,324,989	4,624,835,382
Total on-balance sheet items	<u>279,841,369,692</u>	<u>11,632,482,162</u>	<u>291,473,851,855</u>
Off-balance sheet items	<u>30,523,498,460</u>	<u>1,969,962,361</u>	<u>32,493,460,821</u>
Total	<u>310,364,868,152</u>	<u>13,602,444,524</u>	<u>323,967,312,676</u>

Industry distribution of credit exposures

2020	Banks and FIs	Manufacturing	Industry	Retail	Others	Total BDT
Claims on sovereigns and central banks	36,706,487,911				-	36,706,487,911
Claims on banks	11,192,997,458				-	11,192,997,458
Investments					39,279,285,462	39,279,285,462
Claims on corporate	-	103,294,265,675	109,013,396,899		14,401,593,029	226,709,255,603
Claims on consumer				3,166,436,426	1,171,822,400	4,338,258,826
Fixed assets					322,474,322	322,474,322
All other assets					2,880,155,852	2,880,155,852
Total on-balance sheet items	<u>47,899,485,369</u>	<u>103,294,265,675</u>	<u>109,013,396,899</u>	<u>3,166,436,426</u>	<u>58,055,331,065</u>	<u>321,428,915,434</u>
Off-balance sheet items	<u>2,615,957,970</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>30,096,876,500</u>	<u>32,712,834,470</u>
Total	<u>50,515,443,339</u>	<u>103,294,265,675</u>	<u>109,013,396,899</u>	<u>3,166,436,426</u>	<u>88,152,207,565</u>	<u>354,141,749,904</u>
2019	Banks and FIs	Manufacturing	Industry	Retail	Others	Total BDT
Claims on sovereigns and central banks	30,083,846,873					30,083,846,873
Claims on banks	19,595,350,374					19,595,350,374
Investments					16,278,988,469	16,278,988,469
Claims on corporate	-	98,020,118,971	102,080,639,370		15,944,529,940	216,045,288,281
Claims on consumer				3,377,133,861	1,201,508,702	4,578,642,563
Fixed assets					266,899,913	266,899,913
All other assets					4,624,835,382	4,624,835,382
Total on-balance sheet items	<u>49,679,197,247</u>	<u>98,020,118,971</u>	<u>102,080,639,370</u>	<u>3,377,133,861</u>	<u>38,316,762,407</u>	<u>291,473,851,855</u>
Off-balance sheet items	<u>2,603,188,367</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>29,890,272,453</u>	<u>32,493,460,821</u>
Total	<u>52,282,385,614</u>	<u>98,020,118,971</u>	<u>102,080,639,370</u>	<u>3,377,133,861</u>	<u>68,207,034,860</u>	<u>323,967,312,676</u>

Maturity breakdown of credit exposures

2020	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	33,249,200,560	-	-	-	3,457,287,351	36,706,487,911
Claims on banks	6,253,834,976	1,137,535,437	3,801,627,045	-	-	11,192,997,458
Investments	3,747,054,888	11,620,372,128	23,411,661,456	500,196,990	-	39,279,285,462
Claims on corporate	35,763,565,792	64,053,366,165	83,677,243,135	33,499,199,626	9,715,880,885	226,709,255,603
Claims on consumer	356,130,077	33,028,452	195,516,335	1,877,686,454	1,875,897,508	4,338,258,826
Fixed assets	9,350	1,087,441	18,541,030	233,896,263	68,940,238	322,474,322
All other assets	422,072,099	263,259,305	362,467,948	1,820,605,745	11,750,755	2,880,155,852
Total on-balance sheet items	79,791,867,742	77,108,648,928	111,467,056,949	37,931,585,078	15,129,756,737	321,428,915,434
Off-balance sheet items	6,563,502,648	10,567,825,108	14,062,414,061	1,519,092,653	-	32,712,834,470
Total	86,355,370,390	87,676,474,036	125,529,471,010	39,450,677,731	15,129,756,737	354,141,749,904

2019	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	18,603,762,023	-	-	-	11,480,084,850	30,083,846,873
Claims on banks	9,697,459,894	3,784,061,435	6,113,829,044	-	-	19,595,350,374
Investments	4,493,731,577	3,904,426,847	7,880,830,044	-	-	16,278,988,469
Claims on corporate	37,423,465,967	69,413,130,171	72,450,758,164	32,580,341,820	4,177,592,159	216,045,288,281
Claims on consumer	120,593,719	102,605,360	305,935,194	-	4,049,508,290	4,578,642,563
Fixed assets	274,379	561,045	8,581,534	174,463,590	83,019,365	266,899,913
All other assets	1,107,611,785	1,667,405,387	249,319,438	739,262,737	861,236,035	4,624,835,382
Total on-balance sheet items	71,446,899,344	78,872,190,245	87,009,253,418	33,494,068,148	20,651,440,700	291,473,851,855
Off-balance sheet items	6,304,451,298	8,453,120,915	15,859,589,441	1,876,299,167	-	32,493,460,821
Total	77,751,350,642	87,325,311,160	102,868,842,859	35,370,367,315	20,651,440,700	323,967,312,676

	2020 BDT	2019 BDT
Gross Non Performing Assets (NPAs)		
Non Performing Assets (NPAs) to outstanding loans and advances	1,443,438,302	1,398,717,377
Movement of NPAs		
Opening Balance	1,398,717,377	1,475,858,628
Written off during the period	(51,954,331)	(66,485,900)
Recoveries during the period	(24,319,041)	(71,357,027)
Addition during the period	120,994,297	60,701,676
Closing Balance	1,443,438,302	1,398,717,377
Movement of specific provision for NPAs		
Opening Balance	764,289,121	720,084,005
Written off (net off recovery) during the period	(11,285,833)	(34,605,259)
Recoveries during the period	(173,235,946)	(32,703,308)
Provision made during the period	880,645	111,513,683
Closing Balance	580,647,987	764,289,121

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:

	2020 BDT	2019 BDT
Interest rate risk	13,098,484	47,092,514
Equity position risk	-	-
Foreign exchange risk	62,220,780	367,022,181
Commodity risk	-	-
	75,319,264	414,114,695

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 organization and covers a wide spectrum of issues. The Group manages this risk through a control based environment in which processes are documented, authorization 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 publicized 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 and ownership 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:

	2020 BDT	2019 BDT
Capital charge for operational risk	2,155,533,092	2,044,783,647

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 framework requires:

- liquidity to be 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 day timeline 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:

	2020	2019
	BDT	BDT
Liquidity coverage ratio (%)	162.74%	144.27%
Net stable funding Ratio (%)	144.87%	146.20%
Stock of high quality liquid assets	55,936,552,427	42,463,115,077
Total net cash outflows over the next 30 calendar days	34,372,751,846	29,432,300,305
Available amount of stable funding	281,517,858,586	263,893,488,840
Required amount of stable funding	194,325,036,287	180,498,518,329

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:

	2020	2019
	BDT	BDT
Leverage ratio	10.92%	10.58%
On balance sheet exposure	327,614,532,789	309,651,044,472
Off balance sheet exposure	47,183,181,420	47,314,292,815
Total exposure	374,797,714,209	356,965,337,288

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 clawback, 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 clawback 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:

	2020 BDT	2019 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	772	779
Guaranteed bonuses awarded during the financial year:		
Number of employee	838	854
Total amount of guaranteed bonuses	110,468,795	91,059,588
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	2	6
Total amount of severance payments	13,932,030	44,043,899
Total amount of outstanding deferred remuneration (in cash)		19,390,082
Total amount of deferred remuneration paid out in the financial year	16,023,844	10,025,249
Breakdown of amount of remuneration awards for the financial year:		
Fixed and variable	2,796,883,369	2,761,393,813
Variable pay		
Deferred	16,023,844	10,025,249
Non-deferred	378,038,580	365,104,702
	<u>394,062,424</u>	<u>375,129,951</u>