HSBC Holdings plc

Annual Report and Accounts 1994

HSBC

The HSBC Group

Headquartered in London, HSBC Holdings plc is the holding company of one of the largest banking and financial services organisations in the world. The HSBC Group's international network comprises more than 3,000 offices in 68 countries, operating under well-established names in the Asia-Pacific region, Europe, the Middle East and the Americas. The Group is strongly represented in the United Kingdom and continental Europe, where it has some 1,900 offices in 19 countries, and in Asia with around 600 offices in 20 countries.

With a dual primary listing on the London and Hong Kong stock exchanges, shares in HSBC Holdings plc are held by some 180,000 shareholders in more than 90 countries. In the United States, HSBC Holdings plc offers investors a sponsored American Depositary Receipt programme.

Through a global network linked by advanced technology, the Group provides a comprehensive range of financial services: retail and corporate banking, trade services, investment banking, private banking, trustee services, pension and investment fund management, treasury and capital markets services, consumer and business finance, securities and custody services, and insurance.

HSBC Holdings plc
Incorporated in England with limited liability
Registered in England: number 617987

Registered Office and Group Head Office
10 Lower Thames Street
London EC3R 6AE
United Kingdom

Registrars
Principal Register
The Royal Bank of Scotland plc
Registrar's Department
PO Box 435, Owen House
8 Bankhead Crossway North
Edinburgh EH11 4BR
United Kingdom
Telephone: 0131-523 6131

Hong Kong Overseas Branch Register
Central Registration Hong Kong Limited
19th Floor, Hopewell Centre
183 Queen's Road East
Hong Kong
Telephone: 2862 8628

Stockbrokers
Cazenove & Co.
12 Tokenhouse Yard
London EC2R 7AN
United Kingdom

James Capel & Co. Limited
Thames Exchange
10 Queen Street Place
London EC4R 1BL
United Kingdom

ADR Depositary
Morgan Guaranty Trust Company of New York
PO Box 8205, Boston
MA 02266-8205
USA
Telephone: 617-774 4237

Financial Highlights

1993		1994	*1994*	*1994*
£m	**For the year**	**£m**	*HK$m*	*US$m*
2,584	Profit before tax	**3,166**	*37,527*	*4,857*
1,806	Profit attributable	**2,053**	*24,334*	*3,149*
594	Dividends	**703**	*8,332*	*1,078*
	At year-end			
9,334	Shareholders' funds	**10,790**	*130,397*	*16,854*
16,510	Capital resources	**18,098**	*218,714*	*28,269*
157,088*	Customer accounts and deposits by banks	**147,834**	*1,786,573*	*230,916*
207,447*	Assets	**201,518**	*2,435,345*	*314,771*
124,717	Risk-weighted assets	**125,823**	*1,520,571*	*196,536*
Pence	**Per share**	**Pence**	*HK$*	*US$*
71.13	Earnings	**79.60**	*9.43*	*1.22*
68.77	Headline earnings	**76.84**	*9.11*	*1.18*
23.50	Dividends	**27.00**	*3.26†*	*0.42†*
369.22	Net asset value	**414.04**	*50.04*	*6.47*
	Number of ordinary shares in issue at year-end			
1,707m	HK$10	**1,754m**		
821m	£0.75	**852m**		
%	**Ratios**	%		
20.8	Return on average shareholders' funds	**20.4**		
1.1	Post-tax return on average assets	**1.1**		
	Capital ratios			
13.2	— total capital	**14.4**		
7.9	— tier 1 capital	**9.1**		
55.2	Cost:income ratio	**59.9**		

* *Figures have been restated to conform with the new UK reporting requirements applicable under Financial Reporting Standard 5, 'Reporting the Substance of Transactions'.*

† *The dividends per share are translated at the closing rate. Shareholders who receive dividends in Hong Kong dollars received an interim dividend of HK99.6 cents per share. The proposed final dividend of 19 pence per share will, where required, be converted into Hong Kong dollars at the exchange rate on 15 May 1995.*

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Group Chairman's Statement

The 1994 performance of the HSBC Group was satisfactory, given the difficult conditions in the treasury and capital markets, coupled with increased competition generally. Profit attributable to you, our shareholders, increased by 14 per cent to £2,053 million (HK$24,334 million, or 18 per cent).

Your directors have recommended a final dividend of 19 pence per ordinary share which, together with the interim dividend of 8 pence, will make a total distribution of 27 pence per share for the year. This represents an increase of 15 per cent over 1993. In Hong Kong dollar terms the increase is 21 per cent using the 1994 year-end exchange rate of HK$12.085 to translate the final dividend. The dividend will be payable on 30 May 1995 in cash, in sterling or in Hong Kong dollars, with a scrip alternative.

Despite intense competition, our Group continued to prosper in 1994, aided by the expanding economies in many of our markets, particularly in the Asia-Pacific region where exports and intra-regional trade continued to grow.

In commercial banking, our renewed commitment to providing the highest levels of service to our customers yielded positive results. HongkongBank recorded strong profit growth in almost all countries in which it operates. Its 61.48 per cent-owned subsidiary, Hang Seng Bank, also performed well, and the newly-incorporated Hongkong Bank Malaysia produced results that were above expectations in its first year of operation.

Midland Bank's domestic UK banking business reported an 11 per cent rise in operating profit before provisions, while in North America, Marine Midland's record year was achieved despite weakness in New York State's economy, and Hongkong Bank of Canada's steady growth continued.

We benefited from a significant reduction in doubtful debt provisions thanks in part to significant recoveries in HongkongBank and Midland Bank. Concord Leasing continued to provide for its aircraft portfolio, but at a lower level than in 1993. On 1 January 1995, to obtain business synergies, Concord was merged into Marine Midland Bank.

HSBC Investment Banking, which comprises our merchant banking, equity securities and asset management activities, reported favourable results against a backdrop of volatile markets.

The results of our treasury and capital markets operations in 1994 were disappointing, particularly when compared with the exceptional performance in 1993. After a very difficult first half, there was a modest recovery in the second half of the year.

Risk is inherent in all financial services businesses, and controlling it is central to success. Limits on both credit and market risks are set at levels appropriate for the size of the Group and of the Group entities engaging in transactions with customers and market counterparties.

1994 was a year marked by integration and consolidation. We continued to obtain synergy benefits from the acquisition of Midland Bank. A number of Group companies and lines of business adopted new names which reflect their membership of the HSBC Group: HSBC Asset Management, HSBC Markets, HSBC Securities, HSBC Investment Banking and HSBC Greenwell are but a few examples. In addition, as Marine Midland launched a new image programme, it adopted the Group hexagon logo.

Our Group made further advances in banking technology. Our electronic banking system, Hexagon, attracted its 10,000th customer, and our international ATM network, GlobalAccess, was linked to that of Wells Fargo Bank in California. Group customers now have access to some 210,000 cash machines in 85 countries.

Group Chairman's Statement *(continued)*

Midland Bank is a leading participant in the drive to develop an electronic cash wallet, Mondex. A demonstration centre was opened in Swindon, England, where full-scale testing with local retailers will begin in the summer of 1995. HongkongBank will franchise Mondex in Hong Kong, China, India, Indonesia, Macau, the Philippines, Singapore, Sri Lanka, Taiwan and Thailand, and Hongkong Bank Malaysia will do so in Malaysia.

This *Annual Report* contains a special feature focusing on the HSBC Group's activities in social and environmental spheres.

During 1994 our Group supported community programmes by donations, sponsorships, secondments, in-kind contributions and other community-related efforts to a value of more than £11 million.

I wish to express my warm thanks to all our staff for their hard work and commitment, not only for their day-to-day contributions to our business success, but, in many cases, for their tireless support of volunteer and charitable causes in their local communities.

It was gratifying to see that more than 29,000 staff members in over 40 countries demonstrated their commitment to the Group by subscribing to our savings-related share option scheme, one of the most ambitious schemes of its kind ever devised. A second offer commences in March 1995, and I look forward to repeated success.

As Mr Donald P H Liao recently retired from the HongkongBank Board, he stepped down from our Board of Directors, and we thank him for his valuable service. Sir Adrian Swire joined the Board on 24 February 1995.

Since we established HSBC Holdings in 1991, our Group has experienced much growth and change. We are undeniably a major player on the world's financial stage. Yet despite our size and global capabilities, we are not as well known in some of our markets as we would like to be. Throughout 1995 we shall try to rectify this and have commenced with an advertising campaign in the UK press. Many of our subsidiaries are household names in their respective markets. We would like the same to be said of HSBC, *A World of Financial Services.*

The outlook for 1995 remains challenging, but our diverse product lines, geographic spread, investment in technology and training, and commitment to quality customer service position us well for further growth. With the continued support of our shareholders, customers and staff, we shall achieve further growth.

Sir William Purves, *Group Chairman*
27 February 1995

Group Chief Executive's Report

Despite intense competition in commercial banking around the world and difficult money markets in key financial centres, HSBC produced a satisfactory result in 1994.

1994 Results

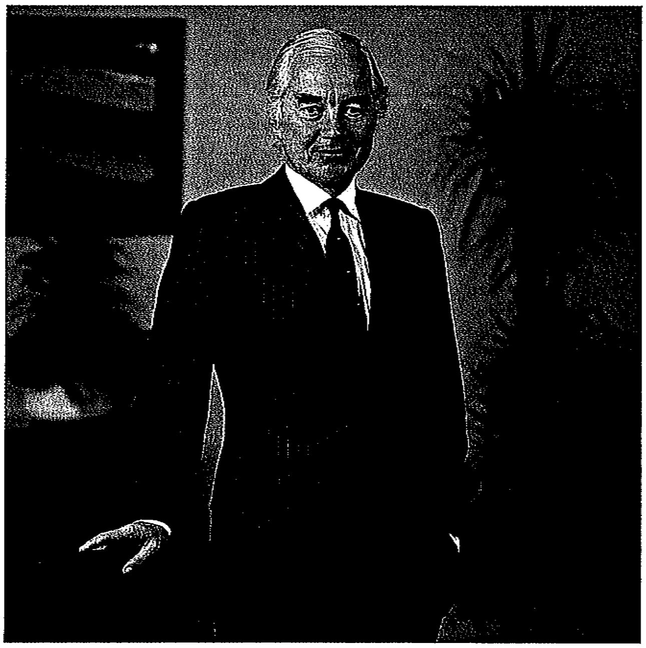
The pre-tax profit of £3,166 million in 1994 represented an increase of 23 per cent over 1993. Our tax charge increased by 61 per cent to £829 million leaving shareholders with an increase of 12 per cent in earnings per share which enabled us to pay a dividend of 27 pence per share, 15 per cent more than 1993.

The Group retained 66 per cent of net profits to maintain a strong capital base which will support the long-term growth of our business.

You will find details of the performance of our major subsidiaries and lines of business after my report.

Results Commentary

Operating income declined by 5 per cent; an encouraging growth in net interest income, with higher fees and commissions, was overshadowed by a substantial decline in dealing profits to £261 million from their exceptionally high level in 1993. With hindsight, it is evident that 1993 was an extraordinary year for trading activities which is unlikely to recur for some time.



However, foreign exchange profits remained good, buttressed by strong retail flows around the world.

We reduced dramatically our proprietary positions in interest rate trading after losses of £92 million in the first half of 1994. We now intend to emphasise making markets in interest rates for our institutional and corporate customers rather than taking proprietary positions.

Operating expenses rose by 3 per cent in 1994 to £4,564 million. However our cost:income ratio rose to 59.9 per cent mainly because of the decline in dealing profits. While our staff are our most valuable resource, they are also the key driver of our expenses. During 1994 our staff increased by 3 per cent. Our policy is to add staff wherever better service, revenue or risk control is the result and to avoid increases in other areas.

A major factor contributing to our satisfactory performance was a sharp reduction of 76 per cent in bad and doubtful debt charges to £275 million. This is due partly to an improvement in the economic environment and partly to the continued shift towards consumer lending in our portfolios. Releases of prior-year provisions amounting to £494 million and recoveries of £124 million from loans which had been written off, contained the level of doubtful debt charges and bear testament to our cautious policy of provisioning in prior years.

All loans in our portfolio are graded according to risk; the trends of this grading system in the portfolio during 1994 were favourable. As a result, total provisions at the end of the year were 3.1 per cent of total customer loans, compared with 3.8 per cent at the end of 1993.

The effective tax rate was 26.2 per cent compared with 1993's rate of 19.9 per cent. More of our taxable profits were earned in countries with higher tax rates, such as the United Kingdom and United States of America, and most of the tax losses in Midland Bank and Marine Midland Bank were utilised in 1993.

Our balance sheet declined by 3 per cent, partly due to a reduction in debt securities and partly as a result of the appreciation of sterling against the US dollar. Geographically, our assets in Asia, both in Hong Kong and other areas, grew faster than the UK and USA, reflecting the different rates of economic growth.

Global Business

The majority of our profits are derived from domestic commercial banking operations around the world, but we have increased our commitment to the very important business lines which serve customers whose needs transcend national boundaries.

Investment banking accounts for 4 per cent of our assets and 9 per cent of our profits. During 1994 HSBC Investment Banking strengthened its position in key markets and expanded its geographic reach by opening in India, Pakistan and South Africa; it offers a very high level of global product expertise, such as Aviation Finance and Export and Project Finance, which capitalise on the Group's strengths and offer enhanced service to the Group's clients in co-operation with the commercial banks.

The unique capabilities of HSBC Investment Banking in Asia were extended by the reorganisation of its institutional equity and treasury activities.

Our insurance business is an important source of non-interest income. We remain committed to developing it, both internally and by acquisition, where appropriate. During 1994 agreement was reached to acquire Lombard Insurance Company Limited in Hong Kong, which will add considerably to our market share in a growing but competitive underwriting market in the region.

Securities custody services continue to grow very satisfactorily. We are well positioned to service institutional investors as they diversify portfolios internationally.

Financing trade has been at the heart of the Group since its origins in Hong Kong and Shanghai in 1865. It remains so today. We continue to enhance the technological support for our trading customers by pioneering Electronic Data Interchange in the USA, the UK and Hong Kong and by upgrading our electronic banking system, Hexagon. We announced the formation of Wells Fargo HSBC Trade Bank in California to further develop our strategic alliance with Wells Fargo & Co. and to provide customers of both banks with trans-Pacific trade finance.

In Group Headquarters we have a small Global Banking Services team who are responsible for product development and co-ordination in our commercial banks, and for transmitting service enhancements and 'best practices' around the Group.

Developing Our Key Resource

The competitive arena of banking is changing fast, which means we have to adapt. We have to identify the changing needs of our customers and then equip and train our staff to meet those needs.

An essential ingredient of our success is the training and development of our 108,321 staff around the world.

In August 1994 we opened our new Group Management Training College in Hertfordshire, UK, underlining our commitment to having management who are capable of leading the change, both in improving customer service and streamlining our internal organisation.

All new executive trainees in the Group come to the College for induction training, when we introduce them to the Group's values, standards, products and computer systems; also this allows us to establish a network of global contacts amongst new executives to supplement those existing amongst middle and senior management.

Having invested in training our executives, it is vital for both the individual and the Group to derive maximum value from their expertise. We maintain a programme of international secondments to spread the expertise and to broaden our executives' work experience; this enables us to develop a cadre of internationally experienced managers to assume senior management positions throughout the organisation. In a world which is shrinking as a result of changes in communications and technology, there is a lot to be gained from practical knowledge of the different banking systems around the world.

Business Environment

Growth in the HSBC Group's earnings is dependent on the health of the economies where we operate. The balance between the high growth economies of Asia and the more mature economies of the West should produce stable earnings growth that would not necessarily be possible from operations concentrated in one country.

We are conscious of the volatility of earnings streams from money-market related sources. We aim to have them account for only a reasonable portion of overall operating income.

Notwithstanding the diversity of our income, the Group depends on effective management of credit and market risk. We are evaluating continuously ways of improving our risk management. We describe our processes in more detail on pages 37 to 42.

We receive a steady flow of new rules, standards and directives. During 1994 the Group has complied throughout the year with the operative provisions of the Code of Best Practice in the Report of the Committee on the Financial Aspects of Corporate Governance (the Cadbury Committee). This year we have changed our accounting policy for the translation of the results of overseas subsidiaries, associates and branches. Their results are now translated using average rates of exchange, whereas previously the rates of exchange in effect on the year-end date were used. We believe that this method more fairly reflects the contribution of these overseas operations to the Group's results. The Group has also complied with new requirements introduced during the year into the listing rules of the London and Hong Kong stock exchanges.

We have provided voluntarily detailed disclosure of directors' remuneration and stock options later in this *Annual Report.*

The Future

Our Group believes that growth is the right strategy to satisfy the aspirations of our customers, shareholders and staff. Growth is achieved best by taking a long-term view of the Group's relationship with its customers; by investing in systems (for example, our unified Treasury system TREATS which underpins major dealing rooms in 22 countries); in products (Mondex — the potential 'smart card' to replace cash); by investing in branches where we meet our customers (major refurbishment programmes in Midland Bank and Marine Midland Bank, new upmarket branches in Hong Kong) and by deepening the relationship we have with over 25 million customers in 68 countries. This is our formula for the future as we continue to offer *A World of Financial Services.*

J R H Bond, *Group Chief Executive*
27 February 1995

Five-year comparison

At year-end *(£m)*	1990*	1991*	1992*	1993	**1994**
Share capital	1,079	1,120	2,054	2,111	**2,090**
Shareholders' funds	4,318	4,819	8,011	9,334	**10,790**
Capital resources	6,232	6,336	13,005	16,510	**18,098**
Customer accounts	51,132	59,996	119,674	128,843	**128,707**
Loans and advances	59,649	64,536	132,194	143,465	**140,739**
Total assets	77,361	85,786	185,141	207,447	**201,518**
For the year *(£m)*					
Operating profit before provisions	1,088	1,326	2,024	3,588	**3,060**
Provisions for bad and doubtful debts	(592)	(529)	(905)	(1,158)	**(275)**
Pre-tax profit	566	920	1,465	2,584	**3,166**
Profit attributable to shareholders	292	611	1,027	1,806	**2,053**
Dividends	(175)	(221)	(472)	(594)	**(703)**
HK$/£ average exchange rate	13.900	13.749	13.664	11.582	**11.853**
Per ordinary share *(pence)*					
Earnings	17.99	37.26	51.74	71.13	**79.60**
Headline earnings	14.42	30.00	39.75	68.77	**76.84**
Dividends	10.86	13.57	19.00	23.50	**27.00**

** Figures for 1990, 1991 and 1992 have been restated to reflect the change in accounting policy for the translation of the results of overseas branches and subsidiary and associated undertakings at average exchange rates, but have not been restated to reflect the new UK reporting requirements applicable under Financial Reporting Standard 5, 'Reporting the Substance of Transactions'.*

Figures for 1990 and 1991 have not been restated to reflect the UK reporting requirements applicable under the Companies Act 1985 (Bank Accounts) Regulations 1991; Financial Reporting Standard 3, 'Reporting Financial Performance'; and Financial Reporting Standard 4, 'Capital Instruments'.

Geographical performance

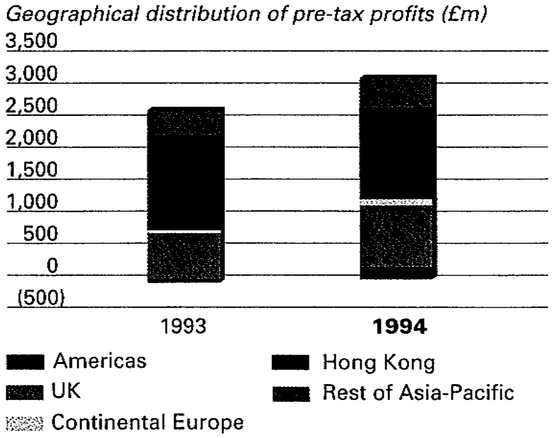
The Group made a pre-tax profit of £3,166 million in 1994, an increase of 23 per cent over 1993. The proportion of pre-tax profits earned in Europe and North America increased, as charges for doubtful debts fell sharply, reflecting the improvement in those economies.

The Group's operations in the United Kingdom made pre-tax profits of £982 million, an improvement of £264 million compared with 1993. Midland Bank benefited from a sharp fall in its bad and doubtful debt charge, which was offset by reduced dealing profits in Midland Global Markets and the UK branch of HongkongBank. A reduction in provisions for contingent liabilities, profits from the disposal of part of the investment in 3i Group and gains made on venture capital investments contributed to the overall improvement in UK pre-tax profit.

Pre-tax profits from the Group's operations in continental Europe recovered to £94 million in 1994, principally as a result of the £120 million reduction in the doubtful debt charge in Midland's subsidiaries in France and Germany. However, this was partly offset by a fall in dealing profits of £85 million.

Pre-tax profits in Hong Kong declined by £88 million. Loan demand remained strong, leading to an increase in net interest income of £82 million. Lower dealing profits contributed to a decline in non-interest income of £158 million. Operating expenses rose by 6 per cent, reflecting an increase in staff costs.

Geographical distribution of pre-tax profits (£m)



In the rest of Asia-Pacific, pre-tax profits rose to £478 million, up £70 million over 1993. As a result of increased customer lending in South-East Asia and New Zealand, net interest income increased by £65 million. Doubtful debt charges were lower by £36 million, mainly in Singapore, Australia and Japan.

In the Americas, pre-tax profits were £177 million, up by £244 million over the loss reported for 1993. Operating income improved following a slight improvement in net interest income and a sharp fall in the amortisation of mortgage servicing rights by Marine Midland. Reduced staff and premises costs and lower charges for doubtful debts contributed to the improved performance in the Americas.

The geographic analysis of pre-tax profits is set out in further detail on pages 77 to 78.

Attributable profit by subsidiary and by line of business

£m	**1994**	1993
i By subsidiary		
Hang Seng Bank Limited	**626**	587
Less minority interests	**(241)**	(226)
	385	361
HongkongBank of Australia Limited	**6**	14
HSBC Investment Bank Asia Holdings Limited	**51**	93
HongkongBank and other subsidiaries	**769**	722*
HongkongBank and subsidiaries	**1,211**	1,190
Midland Bank plc	**595**	646†
— preference dividend	**(13)**	(3)
	582	643
Marine Midland Banks, Inc.	**150**	117
— preference dividend	**(4)**	(4)
	146	113
The British Bank of the Middle East	**51**	61
Hongkong Bank Malaysia Berhad	**44**	—*
Hongkong Bank of Canada	**41**	32
Concord Leasing, Inc.‡	**(128)**	(162)
Other	**106**	(71)
Group profit	**2,053**	1,806
ii By line of business		
Commercial banking	**1,864**	1,707
Investment banking	**189**	173
Provision in respect of British & Commonwealth litigation	**—**	(74)
Group profit	**2,053**	1,806

** Hongkong Bank Malaysia's attributable profit was included in HongkongBank for 1993 (£51 million).*

† Midland Bank's attributable profit for the year to 31 December 1993 included £26 million relating to Samuel Montagu for the first six months of 1993. Samuel Montagu is included under 'Other' for the year to 31 December 1994.

‡ On 1 January 1995, Concord Leasing became a subsidiary of Marine Midland.

Commercial Banking

The Hongkong and Shanghai Banking Corporation Limited

Despite rising interest rates, high inflation and a downturn in the stock and property markets, Hong Kong's economy continued to expand steadily in 1994, supported by the strengthening of some of its key overseas markets and by infrastructure spending. The territory achieved GDP growth of 5.5 per cent in real terms. Most other countries in the Asia-Pacific region continued to grow strongly, fuelled by robust domestic demand, increased intra-regional trade and continued infrastructure development.

In 1994, HongkongBank and its subsidiaries reported an attributable profit of HK$18,907 million, an increase of 39.1 per cent on HK$13,593 million recorded in 1993. This result includes the exceptional profit of HK$4,559 million arising from the sale, subsequent to its local incorporation, of HongkongBank's Malaysian banking business in January 1994 to a fellow subsidiary of HSBC Holdings. Excluding the effect of the sale from the 1994 results and the profits of the Malaysian business from the 1993 figures, attributable profit rose by HK$1,473 million, or 11.4 per cent, to HK$14,348 million and provided a return on shareholders' funds of 28.6 per cent.

Total assets at year-end were HK$1,079 billion, a decrease of 4.6 per cent from 1993. Allowing for the sale of the Malaysian business, the decrease in total assets was 1.5 per cent, with growth in advances to customers in Hong Kong and elsewhere in the Asia-Pacific region offset by the continued integration within Midland Bank of treasury business in London and New York, resulting in a lower level of treasury assets.

Financial highlights*	1994†		1993‡	
	£m	HK$m	£m	HK$m
Share capital and reserves	4,247	51,339	4,161	47,522
Profit before taxation	2,135	25,303	1,735	19,810
Profit attributable to shareholders	1,595	18,907	1,190	13,593
Dividends paid and proposed	1,189	14,090	701	8,000
Total assets	89,245	1,078,978	99,088	1,131,567
Return on average shareholders' funds (%)	28.6		30.1	
Total capital ratio (%)	14.9		14.4	

* *Figures for HongkongBank and its subsidiaries.*
† *On 1 January 1994, HongkongBank sold its Malaysian banking business to a fellow subsidiary of HSBC Holdings plc. The 1994 profit figures shown above include an exceptional gain of HK$4,559 million arising from that sale. This profit is excluded in calculating the return on average shareholders' funds.*
‡ *Figures include the results of the Malaysian banking business.*

Operating income was HK$32,435 million, compared with HK$34,653 million in 1993. The cost:income ratio was 42.7 per cent, compared with 38.8 per cent in 1993, largely due to the reduction in other operating income due to a decline in dealing profits as a result of adverse conditions in the capital markets, particularly in the first half. With the improved quality of the bank's loan book and the write-back of earlier provisions in Hong Kong and elsewhere, the net charge for doubtful debts dropped sharply to HK$174 million from HK$3,850 million.

HongkongBank itself reported a profit after tax of HK$16,656 million, an increase of 45.2 per cent on HK$11,468 million in 1993. Excluding the results of the Malaysian banking business in 1993 and the effects of its sale in 1994, profit rose by 12.5 per cent to HK$12,097 million from HK$10,757 million.

Competition intensified in virtually all of the bank's areas of operation, while cost pressures remained a feature in many markets. The bank responded by focusing its retail efforts in Hong Kong on expanding its relationships with higher-income and middle-market customers, reorganising its treasury and capital markets business, and shifting certain functions to less expensive office space. In other markets, the bank expanded its retail activities such as credit cards and premium banking services and wholesale activities such as securities custody services. Strict cost control measures were continued in all locations.

Hong Kong was again the major contributor to HongkongBank's overall results. Lower loan provisions and sustained economic activity helped to offset the reduced level of dealing profits. Deposit growth was satisfactory. The net interest margin was largely maintained. Loan demand was robust in the first half but levelled off later in the year as the bank's residential mortgage business declined.

In the retail sector, several new products were launched to serve the needs of higher-income customers. The bank's credit card business continued to show healthy growth. The initial deregulation of retail time deposits, which began in October, had little impact on earnings. The bank acquired the rights in

Hong Kong and elsewhere in the Asia-Pacific region to franchise Mondex, a 'smart card' system based on electronically-stored money being developed by Midland Bank and National Westminster Bank.

A new dealing room operating under the HSBC Markets name was opened in HongkongBank's headquarters building in Hong Kong. The largest dealing room in Asia outside Japan, it integrated the capital markets, foreign exchange and treasury businesses of HongkongBank and HSBC Investment Bank Asia (formerly Wardley). As a result of difficult trading conditions in world markets, dealing profits fell significantly in the early part of the year, but recovered modestly in the second half. The establishment of HSBC Markets in Hong Kong raised the bank's profile and increased business turnover in both traditional and off-balance-sheet treasury and capital markets instruments.

In China, the bank produced good results due to an expansion in commercial activity and growth in all sectors of its business. A treasury centre was established in Shanghai and government approval has been sought to purchase a 14-storey building in Guangzhou to house a number of back-office functions currently carried out in Hong Kong.

In Singapore, profits increased with a higher level of fee income from the securities business, credit facilities and card products. The adverse effect of difficulties in the capital markets in the first half was offset by releases of doubtful debt provisions in the latter part of the year. Other operations in the Asia-Pacific region also performed well, particularly in Japan, Brunei, Thailand, Indonesia and Sri Lanka. New branches were opened in Brunei, Hong Kong, Indonesia, Mauritius, Pakistan, Sri Lanka and Taiwan. In Vietnam, permission was received to apply for a branch licence in Ho Chi Minh City.

As the HSBC Group continued to rationalise its business in Europe and the Americas, the contribution of HongkongBank's branches in the United Kingdom and the United States declined. In London, the bank sold its 26-storey building, which had been badly damaged by a bomb in 1993. In the Americas, the bank is transferring certain offices to other HSBC Group members or affiliates to improve customer service, reduce overheads and focus on wholesale activities and its traditional Asian markets. In New York City, six retail branches were transferred to Marine Midland Bank; in Panama, its two branches are being transferred to Midland Bank; and in California, two branches and two representative offices are to be transferred to Wells Fargo HSBC Trade Bank, a newly-formed joint venture between the Group and Wells Fargo & Co.

HongkongBank's subsidiaries reported mixed results in 1994. In Hong Kong, **Hang Seng Bank Limited** (61.48 per cent owned by HongkongBank) reported a 10.6 per cent increase in attributable profit to HK$7,415 million, and **HSBC Investment Bank Asia Holdings Limited** (formerly Wardley Holdings Limited) reported an attributable profit of HK$601 million, compared with HK$1,063 million in 1993. **Carlingford Insurance Company Limited**'s results benefited from strong income growth.

In Australia, **HongkongBank of Australia Limited** reported a reduction in attributable profit to A$12 million, compared with A$30 million in 1993, largely due to difficult trading conditions.

HongkongBank's finance subsidiaries, **Wayfoong Mortgage And Finance (Singapore) Limited** in Singapore and **Mortgage And Finance Berhad** in Brunei continued to report satisfactory results. In Hong Kong, however, **Wayfoong Finance Limited** recorded a downturn in profits due to higher funding costs and reduced loan demand.

Hang Seng Bank Limited

Hang Seng Bank Limited (Group interest 61.48 per cent) and its subsidiaries reported a pre-tax profit of HK$8,483 million for 1994, an increase of 11.9 per cent on HK$7,582 million recorded in 1993. Profit attributable to shareholders was HK$7,415 million, an increase of 10.6 per cent over 1993. The increase was due to a higher operating profit and gains realised from the disposal of investments in locally-listed equities and foreign government bonds.

Operating results benefited from growth in advances to customers and an increase in fees and commissions, but were adversely affected by the narrowing of interest spread and the elimination of exchange gains following the introduction of revised Hong Kong dollar note settlement arrangements.

Loans and advances to customers, net of provisions, rose to HK$115,532 million, an increase of 23.4 per cent. The main sources of growth were trade financing, corporate lending and mortgages.

Financial highlights	1994		1993	
	£m	HK$m	£m	HK$m
Share capital and reserves	2,941	35,547	2,918	33,328
Profit before taxation	716	8,483	664	7,582
Profit attributable to shareholders	626	7,415	587	6,702
Dividends paid and proposed	438	5,196	279	3,187
Total assets	25,169	304,172	24,451	279,224
Return on average shareholders' funds (%)	21.5		21.2	
Total capital ratio (%)	25.2		29.3	

A continued improvement in the quality of the bank's loan book reduced the net charge for doubtful debts to HK$41 million against HK$118 million in the previous year. This improvement was illustrated by a fall in the ratio of non-performing loans and advances from 0.9 per cent to 0.7 per cent of total loans.

The cost of funds came under pressure from intensified competition and the phased removal, from October, of an interest cap on time deposits. During the year, however, net interest income improved as a result of strong growth in advances to customers and a better yield on the bank's interest-free funds. This performance was achieved despite a narrowing of the spread between the best lending rate and the savings rates by 25 basis points. Income was also helped by a higher loan-to-deposit ratio and a better yield on the bank's non-deposit free fund.

Non-interest income was boosted by a substantial growth in fees and commissions arising from credit facilities, trade financing and credit card services.

Higher marketing expenditure and a larger staff led to an increase in operating expenses. However, healthy income growth helped the bank to maintain a low cost:income ratio of 28.7 per cent, only a marginal increase from 27.1 per cent in 1993.

The bank continued to improve services and broaden its customer base. During the year, seven new branches were opened in Hong Kong, bringing the total number to 135. New services, such as the Bank Smart integrated account, were launched to target young professionals and executives. At the same time, the bank continued to focus on automation and the streamlining of work procedures as a means of enhancing customer care and productivity.

Midland Bank plc

The performance of the UK economy last year exceeded most expectations. Growth of close to 4 per cent was faster than forecast and the best since 1988; retail price inflation, at 2.5 per cent, was lower than expected. Despite two increases in the last four months of the year, base rates, which ended 1994 at 6.25 per cent, remained at historically-low levels, coupled with the best inflation record for 30 years.

Midland Bank made a pre-tax profit of £905 million in 1994, an increase of 7.2 per cent on £844 million in 1993. UK Banking's operating profit before provisions from continuing operations increased by 11.2 per cent to £643 million.

Financial highlights	1994 £m	1993 £m
Share capital and reserves	2,858	2,670
Profit before taxation	905	844
Profit attributable to shareholders	595	646
Dividends paid and proposed	413	403
Total assets	80,375	76,473*
Return on average shareholders' funds (%)	21.2	25.6
Total capital ratio (%)	11.5	11.3

** 1993 comparative figure restated to conform with current year's presentation*

Compared with 1993, operating income from continuing operations declined by 13.1 per cent, or £465 million. There was a £44 million, or 2.5 per cent, increase in net interest income and a £509 million, or 28.7 per cent, decrease in other operating income. This decrease was due to difficult trading conditions in the treasury markets. Operating expenses at £2,166 million were almost flat, increasing by only 1.4 per cent on 1993. The charge for bad and doubtful debts declined by £572 million to £98 million, as a result of the improving domestic economic environment.

Membership of the HSBC Group continued to bring rewards and during 1994 Midland's market share improved. However, competition in both the retail and corporate markets intensified and, in spite of the economic recovery, personal and business lending remained lacklustre.

Renewed emphasis was placed on service quality, and improvements have been introduced promoting greater customer retention and cross-selling. Staff training has also continued to receive priority attention.

In October, Midland Private Banking was introduced for more affluent personal customers. By the year-end, 30 specialised private banking units were operating.

Improved technology was utilised to enhance service standards and to give staff more time to devote to customers.

First Direct, Midland's telephone banking division, now has some 700,000 accounts, compared with 500,000 at the end of 1993. In November, First Direct opened a second, purpose-built building in Leeds to accommodate its continuing expansion.

The personal financial services market had a difficult year, with consumer confidence affected by the poor performance of the stock-market and regulatory issues facing the industry. Nonetheless, Midland remained the market leader in guaranteed equity products.

The cards business produced one of the strong performances of the year, with a good increase in both profitability and market share. This performance was helped by the introduction of a range of innovative products. Development of the 'smart card' initiative, Mondex, continued throughout the year. The card allows electronic cash to be transferred to or from the card by telephone, cash machine or at a retail point-of-sale. It will undergo a full-scale trial in the UK during 1995.

Midland also achieved considerable success in the home mortgage market, with a growth in the value of mortgages in the UK of 16 per cent over 1993.

For a fifth consecutive year, the tariff for small businesses remained unchanged. Demand for loans for good business propositions remained weak, with companies preferring to reduce debt. HSBC Trade Services, the name under which Midland and HongkongBank in the United Kingdom provide trade services, won new customers.

Although Midland Global Markets recorded a disappointing performance compared with the exceptional results of 1993, it continued to provide important support to the bank's corporate and institutional customers.

Midland's international network in Europe and Latin America showed improved profitability. With continental European economies moving out of recession, the bank's business made steady progress during the year, particularly in Greece and Turkey, while **Guyerzeller Bank** and **Trinkaus & Burkhardt** produced satisfactory profits.

The sale of approximately half of Midland's shareholding in 3i Group plc as part of the public flotation of that company resulted in a profit of £64 million.

Forward Trust Group reported a pre-tax profit of £82 million, an increase of 34.4 per cent on £61 million recorded in 1993. **Swan National Leasing** formed an alliance with the bank's credit card business to offer special car purchase terms to Midland cardholders.

Marine Midland Banks, Inc.

The US economy grew by 4 per cent in 1994, but New York State, with its weak labour market, lagged behind the country as a whole. The US Government adopted a more restrictive monetary policy and both long and short-term interest rates rose sharply.

Marine Midland Bank reported an attributable profit of US$229 million in 1994, an increase of 32.4 per cent on US$173 million in 1993. Return on average shareholders' funds rose to 16.5 per cent from 14.1 per cent. The increase in profit resulted from growth within the branch network and in the bank's main lending areas: customer loans grew by 10 per cent and customer deposits 4 per cent. The growth in loans and

Financial highlights	**1994**		1993	
	£m	**US$m**	£m	US$m
Share capital and reserves*	**957**	**1,495**	928	1,371
Profit before taxation	**227**	**348**	101	150
Profit attributable to shareholders	**150**	**229**	117	173
Dividends paid and proposed	**69**	**106**	4	6
Total assets	**11,931**	**18,637**	12,222	18,065
Return on average shareholders' funds (%)	**16.5**		14.1	
Total capital ratio (%)	**17.7**		16.8	

** Including preference shares of US$98 million* deposits generated a US$56 million, or 7.9 per cent, increase in net interest income in 1994 compared with 1993.

Non-accruing loans fell to US$190 million in 1994, down 44.2 per cent from US$341 million in 1993. The ratio of loan loss reserves to total non-accruing loans improved from 102.7 per cent to 168.0 per cent. Marine's capital ratios were strengthened, and compared favourably with other US banks. The total capital ratio stood at 17.7 per cent, compared with 16.8 per cent in 1993.

Expense management remained a keystone of Marine's improved profitability: total expenses fell by 7.5 per cent during the year. Reductions were achieved through cuts in staffing levels, disposal of premises and lower costs related to problem assets.

Marine Midland launched numerous service-quality initiatives during 1994, including a five-year capital expenditure programme for branch refurbishment. The bank also adopted the Group's hexagon corporate symbol. Market share was enhanced by credit card promotions and the acquisition of Spectrum Home Mortgage Corporation.

In addition to its activities in New York State, Marine competes selectively throughout the United States in a number of businesses: student lending, mortgage servicing, credit cards and commercial finance. It is also a key participant in HSBC Group global businesses such as payment services and its electronic financial service, Hexagon.

Hongkong Bank of Canada

The continued growth of Hongkong Bank of Canada was consistent with the sustained expansion of the Canadian economy, which grew by 4.5 per cent in 1994. Although domestic inflation was the lowest in the developed world, short-term interest rates rose by 1.5 percentage points.

Hongkong Bank of Canada reported an attributable profit of C$86 million in 1994, an increase of 35.8 per cent on C$63 million recorded in 1993. Over the same period, return on average shareholders' funds increased by 3.4 per cent, from 13.3 per cent to 16.7 per cent. Loan demand rose by 14.8 per cent, and was particularly strong in the bank's residential mortgage sector, which went up by 25.7 per cent. The bank maintained its traditional conservative credit policies and commercial loans increased by 7.9 per cent. By year-end, the tier 1 capital ratio stood at 5.4 per cent and the total capital ratio 8.7 per cent. Deposits grew by 18.9 per cent.

Charges for loan losses remained below the industry average, with provisions of C$62 million, compared with C$51 million in 1993. The year also saw the completion of the non-accrual loan management that had been part of the purchase of Lloyds Bank of Canada in 1990. Careful administration of this portfolio has yielded benefits to both Hongkong Bank of Canada and Lloyds because of successful recoveries of non-performing loans.

Financial highlights	1994*		1993*	
	£m	**C$m**	£m	C$m
Share capital and reserves	**240**	**526**	254	499
Profit before taxation	**65**	**136**	47	92
Profit attributable to shareholders	**41**	**86**	32	63
Dividends paid and proposed	**29**	**60**	8	15
Total assets	**7,299**	**16,021**	6,885	13,519
Return on average shareholders' funds (%)	**16.7**		13.3	
Total capital ratio (%)	**8.7**		9.1	

** Fiscal year to 31 October*

Hongkong Bank of Canada's trade finance activities increased by more than 19 per cent; in part, this was attributable to the substantial expansion in Canadian exports. Assets reached C$16 billion, an 18.5 per cent increase on C$13.5 billion recorded in 1993. Non-interest expenses rose by 10.7 per cent, from C$252 million to C$279 million.

In the first year of full branch network sales of mutual funds, total funds invested rose by more than 235 per cent, from C$97 million to C$325 million. This growth was due, in part, to low deposit rates early in the year as well as to effective marketing of new investment products.

Hongkong Bank Malaysia Berhad

The Malaysian economy remained buoyant in 1994, with GDP expected to have shown a growth of 8.5 per cent. The economy was driven by a sustained high level of domestic industrial and infrastructure activity, and by stronger external demand following the gradual recovery in the economies of Malaysia's

Financial highlights*	1994	
	£m	M$m
Share capital and reserves	257	1,025
Profit before taxation	73	293
Profit attributable to shareholders	44	178
Dividends paid and proposed	10	42
Total assets	3,144	12,547
Return on average shareholders' funds (%)	21.2	
Total capital ratio (%)	9.8	

** Figures for Hongkong Bank Malaysia and its subsidiaries*

major trading partners. As a result, the manufacturing, construction and service sectors saw robust growth.

Hongkong Bank Malaysia Berhad and its subsidiaries reported an attributable profit of M$178 million in 1994, the first year of operations. HongkongBank's Malaysian operations were transferred to a new Malaysian-incorporated bank, Hongkong Bank Malaysia Berhad, on 1 January 1994. Under the requirements of the act that led to its incorporation, Hongkong Bank Malaysia appropriated M$100 million from its 1994 profits to a reserve fund. In addition, the bank revalued its properties.

Growth in customer advances and deposits was encouraging. Competitive pressures led to finer pricing for advances and, with the cost of funds remaining relatively high, interest margins were squeezed.

However, non-interest income showed satisfactory growth while operating expenses were well-contained. The cost:income ratio was 45.4 per cent.

The British Bank of the Middle East

In 1994, most countries in the Middle East experienced slower economic growth as a result of depressed oil prices. The only exception was Lebanon, an economy which continued to recover with the return of political stability.

The British Bank of the Middle East reported an attributable profit of £51 million in 1994, a decrease of 15.2 per cent on £61 million recorded in 1993. However, the 1993 figure included the bank's share of attributable income from its associated undertaking, The Saudi British Bank, which was sold in that year to another subsidiary of HSBC Holdings. The capital realised on this sale was paid to its parent by way of a dividend. Excluding the results of The Saudi British Bank from 1993, attributable profit in 1994 was 11.4 per cent higher than in 1993, due mainly to an 8.4 per cent growth in net interest income as higher interest rates widened margins. The increased attributable profit was also a result of a 23 per cent rise in net fees and commissions from trade finance earnings. Operating expenses were down 3.0 per cent and bad debts were minimal. Loan demand remained constant.

The bank's total assets decreased by 7.5 per cent compared with 1993. This was largely a result of exchange movements and lower unrealised gains on off-balance-sheet contracts following the maturity of a number of interest rate swaps.

During the year, a fourth branch was opened in Lebanon. Following developments in the Palestinian-Israeli peace process, a representative office was opened in Jericho in the Palestinian Autonomous Area. The bank's new branch in Trivandrum, India, recorded a profit in its first full year of operation.

Financial highlights	1994	1993
	£m	£m
Share capital and reserves	154	147
Profit before taxation	73	90
Profit attributable to shareholders	51	61
Dividends paid and proposed	40	116†
Total assets	3,056	3,305
Return on average shareholders' funds (%)	31.5	29.5
Total capital ratio* (%)	11.7	13.1

** Calculated according to States of Jersey rules, which are, in all material respects, identical to those of the Bank of England. In previous years, the ratio was calculated under Hong Kong Monetary Authority rules.*

† Including £6 million preference dividends

On 15 March 1994, The British Bank of the Middle East's Head Office was relocated to Jersey, which is the major centre for the HSBC Group's private banking business.

Concord Leasing, Inc.

Concord Leasing, Inc. reported a net loss of US$197 million in 1994, compared with a loss of US$244 million in 1993. Operating results were depressed by high levels of non-performing assets and recognition of non-recurring costs associated with positioning Concord for future growth. The loss was compounded by further provisioning due to the erosion of asset

Financial highlights	1994		1993	
	£m	us$m	£m	us$m
Share capital and reserves	3	5	79	117
Loss before taxation	(128)	(197)	(162)	(244)
Loss attributable to shareholders	(128)	(197)	(162)	(244)
Total assets	960	1,499	1,161	1,716

values primarily in Concord's aviation portfolio, which is being phased out.

The company is rebuilding its core equipment financing business in the construction, transportation and communications sectors. In 1994, HSBC Holdings injected US$100 million of additional capital to support Concord's operations and restructuring.

Since June 1994, when Concord moved its headquarters to Buffalo, New York, Marine Midland has provided Concord with back-office support including operations, systems, financial control, credit policy, audit and legal functions. On 1 January 1995, Concord became a subsidiary of Marine.

Associated Commercial Banks

The Saudi British Bank (Group interest 40 per cent) reported a pre-tax profit of SR350 million in 1994, a decrease of 12.9 per cent on SR403 million recorded in 1993. The exceptional results from investments in 1993 were not matched in 1994 and the fall in profits illustrates this fact. Total income from trading and investment securities decreased by SR81 million, or 14.9 per cent, from SR545 million to SR464 million.

Financial highlights	1994		1993	
	£m	SRm	£m	SRm
Share capital and reserves	442	2,592	449	2,500
Profit attributable to shareholders	61	350	72	403
Dividends paid and proposed	45	259	57	317
Total assets	4,627	27,109	4,090	22,765
Return on average shareholders' funds (%)	13.8		21.4	
Total capital ratio (%)	17.3		18.4	

Other areas of the bank performed well despite tightening liquidity in an environment in which the Saudi government reduced public expenditure and real GDP declined. Total loans grew by 19 per cent over the year, from SR8,155 million to SR9,708 million, boosted by increased customer demand for finance in the light of a slow-down in government disbursements. Non-funds income increased by SR30 million, or 29.3 per cent, from SR105 million to SR135 million. Income from foreign exchange activities rose to SR59 million from SR51 million, an increase of SR8 million or 14.9 per cent. Strict cost control measures kept the rise in operating expenses below 2 per cent, amounting to SR342 million from SR335 million in 1993.

The bank's share of deposits increased and it retained its top position in share trading. It is now the Kingdom's third-largest issuer of credit cards.

During the year, the bank launched the first 24-hour, person-to-person direct banking service in the Kingdom. Expatriate banking and remittance services were expanded using Group technology and a private banking service was launched.

The Cyprus Popular Bank Limited (Group interest 21.96 per cent) reported an attributable profit of C£15 million in 1994, an increase of 22.5 per cent on C£12 million recorded in 1993. Its capital adequacy ratio remained high at 12.7 per cent, compared with 13.8 per cent in 1993. The bank increased market share in both deposits and its loan portfolio.

Egyptian British Bank S.A.E. (formerly Hongkong Egyptian Bank) (Group interest 40 per cent) reported an attributable profit of E£16 million in 1994, an increase of 55 per cent on E£10 million recorded in 1993. The cost:income ratio fell from 62.6 per cent to 54.5 per cent and, notwithstanding the increased capital, return on average shareholders' funds improved to 23.8 per cent. Its performance was helped by substantially-increased advances and the abolition of the mandatory central bank tariff on commissions charged by banks. An exceptional depreciation charge of over E£2 million was more than offset by significant bad debt recoveries of nearly E£7 million.

The bank opened a new branch at Maadi, Cairo, and introduced the Group's GlobalAccess automated teller machine service to Egypt.

UBAF Bank Limited in London (Group interest 24.77 per cent) reported a record pre-tax profit of

£29 million in 1994, an increase of 5.4 per cent on £27 million recorded in 1993.

Recoveries of suspended interest and the release of some doubtful debt provisions contributed to an after-tax profit of £21 million. The total capital ratio was 29.8 per cent. Increased income from commercial banking operations compensated for a decline in the refinancing of letters of credit. Total overheads of £11 million were unchanged from 1993. The cost:income ratio fell by 5 per cent to 32 per cent.

The bank opened its first overseas office, in Beirut.

Treasury and Capital Markets

Co-ordinated functionally, the Group's treasury and capital markets operations comprise subsidiaries of, or divisions within, its major commercial banks in which their results are consolidated. These activities — carried out by 42 dealing rooms around the world — encompass foreign exchange, money market, debt securities and derivatives trading, as well as debt underwriting in a wide range of currencies.

The treasury and capital markets operations' results were disappointing in 1994, compared with the exceptional results of 1993. Markets proved extremely difficult, with an unanticipated knock-on effect of rises in US dollar interest rates causing losses in proprietary trading in the first half of the year. Dealing profits improved in the second half, with interest rate trading accounting for much of the turnaround. Corporate and retail foreign exchange continued to provide a strong source of earnings.

A number of strategic restructuring programmes were implemented. A major new dealing room was established in Hong Kong, integrating the strengths of the HongkongBank treasury and Wardley capital markets operations under the **HSBC Markets** name. In Singapore, a capital markets origination and trading unit was set up to market to customers in Malaysia, Indonesia, Singapore and Thailand. Carroll McEntee & McGinley Incorporated changed its name to **HSBC Securities, Inc.** and a new line of business was created under the name **HSBC Futures**, encompassing futures broking businesses of the Group in New York, Chicago, London, Singapore and Sydney.

Treasury sales teams have been expanded across the Group to widen the range of products available to clients.

Private Banking and Trustee

Operating under the functional management of Group Private Banking in Jersey, private banking and trustee units' profits are consolidated in the results of the commercial or investment banking companies. A full range of investment and trust products is delivered through offices in Hong Kong, Singapore, Switzerland, London and Jersey.

In 1994, **HSBC Investment Bank Asia Limited** (formerly Wardley Limited), the Group's principal private banking operation in the Asia-Pacific region, reported reduced earnings, principally due to trading losses. **Guyerzeller Bank AG** (Group interest 74.9 per cent) was adversely affected by write-downs in its investment portfolios as a result of difficult fixed income and equity markets. These results were offset to some degree by strong profit growth in the trustee operations in Hong Kong and Singapore. The private banking operations of **The British Bank of the Middle East** in Geneva also performed well.

The international private banking branches of **Midland Bank** and The British Bank of the Middle East in London, together with **Samuel Montagu** Private Banking, moved into new offices in Mayfair, London, in July. Both Midland and The British Bank of the Middle East maintained profits at a satisfactory level, while Samuel Montagu Private Banking recorded a strong increase in new business and profitability.

Group Private Banking became a division of **HSBC Investment Bank Limited** from 1 January 1995 to exploit the synergies between the origination and distribution sides of the investment banking business.

Insurance

The Group's insurance businesses — including companies such as **Carlingford Insurance Company Limited**, **Gibbs Hartley Cooper Limited**, **Hexagon Insurance Services Limited** and **Midland Life Limited** — engage in life and pension underwriting, insurance broking, employee benefits consultancy, general insurance underwriting, and agency and insurance premium financing. These businesses are co-ordinated functionally by Group Insurance Head Office but are managed through insurance holding companies or within commercial or investment banking subsidiaries.

The markets in which the Group undertakes insurance activities experienced mixed results during 1994. Following a review of pension transfers in the UK by the Securities and Investment Board, Group members operating in the life and pensions sector increased provisions to £47 million to cover potential liability for pension transfers, non-joiners and opt-outs of occupational pension schemes. Non-life markets experienced greater competition as capacity increased following generally improved underwriting experience.

In 1994, the insurance businesses on the whole attained higher levels of profit than in 1993. Life insurance profits were similar to those in 1993.

Agreement was reached to acquire Continental Insurance Corporation's shareholding in Lombard Insurance Company Limited for HK$220 million to complement the Group's non-life underwriting businesses in Hong Kong and expand our presence in Singapore.

The Group's Lloyd's insurance broking subsidiary holding company acquired a 6 per cent stake in the Hogg Group, a fellow Lloyd's broker, but bid unsuccessfully to acquire the whole of the issued share capital. The Group's shareholding was subsequently sold at a profit of £4 million.

Investment Banking

HSBC Investment Banking, which comprises the merchant banking, equity securities and asset management activities of the HSBC Group, reported a pre-tax profit of £229 million, a decrease of 1 per cent from £231 million in 1993. Attributable profit was £189 million compared with £173 million in 1993, a 9 per cent increase. The 1993 figures have been restated to exclude the results of the capital markets trading activities of HSBC Investment Bank Asia, which were merged with HongkongBank's treasury in 1994. Return on average shareholders' funds was 24 per cent.

This satisfactory result in the face of difficult market conditions arose from a consolidation of product expertise, active co-operation with the Group's commercial banks and product and geographical diversification.

A new operating company, **HSBC Investment Bank Limited**, now serves as a marketing unit for this line of business.

From January 1995, Group Private Banking became part of HSBC Investment Banking to extend private client services through a wider range of investment banking products on offer.

Financial highlights	**1994**	1993*
	£m	£m
Share capital and reserves	**739**	848
Merchant banking	**145**	131
Equity securities	**59**	68
Asset management	**25**	32
Profit before taxation	**229**	231
Profit attributable to shareholders	**189**	173
Total assets	**9,123**	13,423
Return on average shareholders' funds (%)	**24.3**	21.8

* *Figures have been restated to exclude the results of the capital markets trading activities of HSBC Investment Bank Asia (formerly Wardley), which were merged with HongkongBank's treasury in 1994.*

To enhance the identity of the Group's investment banking activities, Wardley Holdings Limited changed its name to **HSBC Investment Bank Asia Holdings Limited** on 7 February 1995; most other Wardley Group companies will also incorporate the HSBC initials.

The continental European offices of **Samuel Montagu** are being restructured and will operate under the name HSBC Investment Banking for corporate finance and primary market activities. Two global merchant banking product groups were also formed: HSBC Group Aircraft Finance and HSBC Project and Export Finance.

Merchant Banking

Merchant banking activities made a pre-tax profit of £145 million, an increase of 11 per cent from £131 million in 1993.

Samuel Montagu had a very good year, with strong performances from project and export finance, specialised finance, and from **Montagu Private Equity**. The corporate finance division sponsored 21 flotations, placings and rights issues which raised more than £741 million.

The specialised financing division was co-arranger for the two largest debt financings for management buy-outs in Europe and was active in the syndicated loan market, raising a total of £2 billion for HSBC Group customers in the sterling market alone.

Project and export finance supported a number of major exporting programmes, including the completion of a US$250 million line of credit for China Light & Power in Hong Kong.

Montagu Private Equity benefited from a number of significant gains when companies in which it had investments were either sold or floated. It maintained its position as a leading player in arranging private equity deals and raised its first external investment fund.

The subsidiaries of HSBC Investment Bank Asia Holdings Limited (formerly the Wardley Group) achieved satisfactory results against a background of generally weak Asian equity and bond markets.

HSBC Corporate Finance Limited (formerly Wardley Corporate Finance Limited) sponsored or acted as co-lead underwriter of 20 Hong Kong company flotations, raising approximately HK$10 billion. It was the leading Hong Kong new issue house in 1994.

HSBC Capital Limited (formerly Wardley Capital Limited) remained a market leader in providing specialist project advice in Asia, structuring and advising on many of the key infrastructure projects in the region.

Equity Securities

The equity securities activities of HSBC Investment Banking reported a pre-tax profit of £59 million, a decrease of 13 per cent on £68 million in 1993.

James Capel increased its level of fee income and consolidated its market share. Its commitment to new equity markets for both primary and secondary activities was made evident in the signing of joint venture agreements with Batlivala and Karani in India and Simpson McKie in South Africa. A representative office was opened in Islamabad and the Seoul representative office was upgraded to branch status.

Most UK businesses produced favourable results despite market volatility. Institutional sales, derivatives, corporate bonds and equity capital markets all performed well. Market-making commenced in shares of James Capel's corporate clients and in investment trusts. The private client stockbroking business continued its good performance in spite of difficult market conditions. Poor market conditions in continental European markets led to a downturn in trading income, but agency business was good and James Capel retained its number-two position in European equity research.

Both **Wardley Financial Services Limited** and its subsidiaries and James Capel's Asian operations did well.

James Capel's primary market activities continued to expand with increased activity in India, Latin America and southern Europe. In the UK, new issue activity remained at a high level, with James Capel acting as broker to 16 flotations, including four investment trusts.

Asset Management

HSBC Asset Management, the Group's investment advisory and fund management arm, reported a pre-tax profit of £25 million, a decrease of 22 per cent from £32 million in 1993. Poor market conditions adversely affected both fee income and sales of mutual funds.

Despite a net inflow of funds during 1994, declining world equity markets resulted in the closing figure for funds under management remaining broadly flat at US$31 billion.

The consolidation of the business under the HSBC name, which began in 1993, was completed with the re-branding of mutual fund products. Progress was made in developing a global emerging markets capability, and an International Emerging Markets Fund, a sub-fund of the Luxembourg-based SICAV, was launched in November.

HSBC in the Community

In this year's Annual Report and Accounts, *we broaden our coverage of the HSBC Group's activities. The 'Financial Review' and the 'Review of the Group' remain the core components, but these sections do not fully convey the diversity of the HSBC Group or cover special features of the Group's operations. Hereunder we describe a range of community and environmental projects supported by Group members.*

Companies providing financial services, in particular commercial banks, have a closer relationship with their customers than many other types of businesses. Theirs is a relationship based in large measure on faith and confidence. The HSBC Group aims to earn the trust of its customers by providing services that are competitive, reliable and, above all, responsive to needs.

We believe we repay the trust shown in us by demonstrating our commitment to the communities in which we operate. By supporting communities and working in close partnership with them, we actively contribute to their physical, economic and social well-being. As a business, we naturally wish to see the communities we serve grow and prosper.

How do we help the community? Primarily, we give financial support to charitable, educational, social welfare and environmental projects. As important as money is, it is of little value if it is not used effectively. Frequently, we offer back-up support, and endeavour to provide managerial and financial advice. Our staff often work on community projects.

We sometimes invite other businesses to work with us for the benefit of the community. Pooling resources enables businesses to make a greater impact. For instance, the Private Sector Committee on the Environment, which HongkongBank set up in 1988 to try to tackle Hong Kong's pollution and other environmental problems, is all the more influential and effective for having within its membership many of the territory's largest companies.

Group staff are involved at their own initiative in many different community activities, from helping the elderly to raising funds to literally rolling up their sleeves to improve neighbourhoods.

The 'brush-up' programme is one of hundreds of employee volunteer schemes organised by Marine Midland Bank. Staff and their families spend many hours repainting and improving houses in lower-income communities. Their counterparts in HongkongBank in the Philippines showed great compassion and dedication by raising money for, and distributing food to, the victims of the Mount Pinatubo eruption. Many other staff have given their time and expertise to participate in local community schemes. We are very grateful to them.

Fulfilling aspirations, meeting needs

Each community has its unique characteristics, its own aspirations and special needs. It is our aim to assist in fulfilling those aspirations and meeting those needs. Each Group member runs its own community programme and sets its own priorities. Across the Group, however, there are four broad areas to which special attention is given: education and training, the environment, help for the disabled and disadvantaged, and culture and the arts.

Supporting education and training

Education and training are vital: communities can only progress and prosper if the people within them have the necessary knowledge and skills. The HSBC Group focuses its attention on business and management training. It is our aim to ensure that local businesses in general — not only our businesses — are in a position to recruit from a well-educated pool of graduates and school-leavers.

We promote a number of schemes to this end. Marine Midland Bank is providing a US$1 million endowment for the Marine Midland Centre for International Leadership at the University of Buffalo's School of Management to fund educational and outreach activities in international business and corporate leadership. Hongkong Bank of Canada has endowed the University of British Columbia with C$1 million to set up a professorship in Asian commerce. The Hang Seng School of Commerce, set up by Hang Seng Bank in 1980 as a non-profit-making body, has had more than 3,000 graduates pass through its doors, mostly in business studies.

Several Group members and associates have established scholarship funds for local students:

- The Saudi British Bank sponsors Saudi students to study at a local university after which they are expected to join the bank.
- Egyptian British Bank gives scholarships to Egyptian students studying finance, economics or management subjects.
- In Guam, HongkongBank provides scholarships for business students.
- HongkongBank in Indonesia funds a banking and finance scholarship at the IPMI (Institute Pengembangan Manajemen Indonesia) Management School.
- At any one time, more than 50 Hong Kong students and some mainland Chinese students in Hong Kong benefit from HongkongBank scholarships.

Skills in business and finance are not, however, the only areas we seek to promote. HongkongBank has established the HongkongBank Language Development Fund and chairs the Hong Kong Language Campaign. Both of these schemes seek to ensure that Hong Kong has the language capabilities it needs to maintain its position as one of the world's leading financial centres. Hongkong Bank Malaysia Berhad, too, is active in this area, sponsoring a television series designed to improve English-language business skills.

Adopting a broader approach still, Hongkong Bank of Canada has donated a substantial sum to the University of Toronto to create an archive and research collection covering Hong Kong-Canada relations.

Protecting the environment

Environmental degradation and destruction can threaten to undo much of the good being achieved by economic development. Many Group members support projects to demonstrate the feasibility of maintaining a balance between economic growth and environmental protection.

In Hong Kong, the Private Sector Committee on the Environment, chaired by HongkongBank, has set up a centre to demonstrate clean technologies to industries both in Hong Kong and elsewhere in the region. Anticipating a greatly increased demand for its services, the centre is constructing a new building using state-of-the-art environmental standards. The Committee has also pioneered methods to improve the efficiency of the collection of floating refuse in Hong Kong harbour and worked with the Hong Kong Government to develop an air pollution index.

Midland Bank supports a scheme in the UK to encourage farming methods which minimise environmental damage. The project assists farmers to carry out environmental audits of their farms to improve soil management, crop protection, pollution control and energy conservation. The LEAF (Linking Environment and Farming) Environmental Audit shows that integrating the environment with food production can be profitable as well as desirable.

Additionally, Midland has contributed over £1 million to The National Trust, raised from charges on an affinity card for the Trust. Midland also provides start-up grants for local groups through the British Trust for Conservation Volunteers, made donations to the Woodland Trust and sponsored National Tree Week 1994, the UK's largest annual tree planting and conservation event.

Many wide-ranging environmental projects receive HongkongBank's backing:

- The Care-for-Nature programme in Singapore, in which HongkongBank has been a leading supporter, is helping to turn the island state's Botanic Gardens into one of the world's leading botanical institutions.
- Hongkong Bank Malaysia plays a prominent role in campaigns to protect Malaysia's marine environment. In recognition of its contribution to marine conservation, the bank is the only private sector company appointed to the National Advisory Council on Marine Parks and Marine Reserves. The bank received an environment award from the Malaysian International Chamber of Commerce and Industry.
- HongkongBank co-sponsored the Urban Growth and the Environment Congress in Hong Kong in 1994. This congress brought together experts from many countries to explore the environmental impact of large cities and to propose economically-viable solutions to urban environmental problems.
- The protection of the tiger, an endangered species, is the main focus of HongkongBank's environmental programme in Thailand.

- HongkongBank in Mauritius is providing financial assistance to a fund for the protection of birds under threat of extinction.

- In Brunei Darussalam, HongkongBank supports a scheme to research and maintain the ecosystems of local rain forests.

Helping the disabled and disadvantaged

Giving help to disabled and disadvantaged members of society is an essential part of the HSBC community programme. Group members support a number of organisations working to improve the lives of those with disabilities and to provide them with opportunities for self-advancement:

- HongkongBank has made substantial donations to Hong Kong welfare projects and, in particular, to organisations providing special facilities for the disabled, including the Hong Kong Association for the Mentally Handicapped Hostel and Day Activity Centre. Additionally, the Hongkong Bank Foundation funded and assisted the Hong Kong Medical Association in an innovative campaign to raise awareness of the importance of organ donation.

- Midland Bank sponsors the Summer Action programme in London in which some 5,000 youngsters from disadvantaged areas participate in a range of recreational and educational activities organised by the Metropolitan Police and by local authorities. Midland supports over a dozen charities providing help for the homeless.

- HongkongBank in India contributes to the Happy Home and School for the Blind in Bombay. It is funding mobile crèches for children of migrant construction workers and assisting in the care, treatment and training of disabled children. The bank has also contributed to Mother Teresa's Missionaries of Charity for the underprivileged.

- The British Bank of the Middle East supports a sports championship for the disabled in Bahrain, schemes to assist deaf people in Jordan, and two schools for the handicapped in Dubai.

Sustaining cultures and the arts

A community's culture binds it together, providing a sense of purpose and direction and forging a link between the past and the future. The Group has especially strong ties with Asia, dating from 1865 when HongkongBank was established to finance East-West trade.

We take special pride in our association with cultural events within Asian communities. HongkongBank of Australia is closely involved with the Chinese New Year Festival in Perth, for example. Across the Pacific, Hongkong Bank of Canada provides financial and managerial support for The United Chinese Community Enrichment Services Society, which provides a range of social services for the Chinese community in Vancouver. In India, HongkongBank sponsors the Banganga Festival, an annual musical event held at a site of national heritage in Bombay. And in a number of locations, Group members sponsor dragon boat races and Chinese crafts festivals.

Some major national arts institutions receive HSBC Group assistance. Midland Bank sponsors a series of promenade performances at the Royal Opera House in London. Marine Midland Bank contributes to several arts institutions such as the Lincoln Center for the Performing Arts and the Metropolitan Museum of Art, and supports events of other New York orchestras, including the Buffalo, Rochester, Albany and Syracuse symphonies. Marine is the sole event sponsor of ArtPark in Buffalo. Other orchestras receiving financial support from Group members include the Hong Kong Philharmonic, the Sri Lanka Symphony and the City of London Sinfonia.

Continued commitment

There are many other initiatives supported by the Group or in which Group members are involved, but it is not possible to mention all of them. We hope, however, the range of programmes described on these pages gives a clear indication of our philosophy, our priorities and, above all, our commitment to the well-being of the communities in which we operate, live and work.

Board of Directors and Group General Managers

Directors

Sir William Purves, CBE, DSO, *Group Chairman*
Age 63. Appointed an executive Director and Group Chairman in 1990. Joined HongkongBank in 1954; an executive Director of HongkongBank since 1982 and Chairman and Group Chief Executive Officer from 1986 to 1992. Chairman of The British Bank of the Middle East and of Midland Bank plc and a Director of Marine Midland Banks, Inc. and a non-executive Director of The 'Shell' Transport and Trading Company, plc.

*Baroness Dunn, DBE, *Deputy Chairman*
Age 54. Executive Director of Swire Pacific Limited, a Director of John Swire & Sons (H.K.) Limited and Cathay Pacific Airways Limited. Appointed a non-executive Director in 1990 and non-executive Deputy Chairman in 1992. A non-executive Director of HongkongBank since 1981. Senior member of the Executive Council of Hong Kong.

*Sir Peter Walters, *Deputy Chairman*
Age 63. Deputy Chairman of Thorn EMI plc, non-executive Chairman of Blue Circle Industries plc and of SmithKline Beecham plc and a non-executive Director of Cordiant plc. Appointed a non-executive Director in 1992 and non-executive Deputy Chairman in 1993. Chairman of Midland Bank plc from 1991 to 1994.

B H Asher
Age 58. Executive Director Investment Banking. Appointed an executive Director in 1990. Joined HongkongBank in 1980 and a Director of HongkongBank from 1989 to 1992. Executive Chairman of James Capel & Co. Limited, Chairman of HSBC Investment Bank Limited, Samuel Montagu & Co. Limited and HSBC Investment Bank Asia Holdings Limited and a Director of Midland Bank plc.

J R H Bond
Age 53. Group Chief Executive. Appointed an executive Director in 1990. Joined HongkongBank in 1961; an executive Director of HongkongBank since 1988. President and Chief Executive Officer of Marine Midland Banks, Inc. from 1991 to 1992. Chairman of Hongkong Bank of Canada and a Director of HongkongBank, Midland Bank plc, Hang Seng Bank Limited, Hongkong Bank Malaysia Berhad, The Saudi British Bank, and a non-executive Director of the London Stock Exchange, British Steel plc, Eurorail CTRL Limited and Visa International.

*D E Connolly, OBE
Age 63. Chartered Accountant. A Director of Kowloon-Canton Railway Corporation. A non-executive Director since 1990 and a non-executive Director of HongkongBank since 1985.

R Delbridge
Age 52. Group Finance Director. Appointed an executive Director in 1993. A Director of Midland Bank plc since 1989.

J M Gray
Age 60. Chairman and Chief Executive Officer of HongkongBank. Appointed an executive Director in 1990. Joined HongkongBank in 1952; appointed Executive Director Finance in 1986, Deputy Chairman in 1990, Chief Executive Officer in 1992 and Chairman in January 1993. Vice-Chairman of Hang Seng Bank Limited, and a Director of Swire Pacific Limited and HSBC Investment Bank Asia Holdings Limited. Chairman of the Hong Kong Port Development Board and a member of the Executive Council of Hong Kong, the Governor's Business Council and the Provisional Airport Authority.

*Sir Joseph Hotung
Age 64. A Director of China & Eastern Investment Company Limited and Hongkong Electric Holdings Limited. Appointed a non-executive Director of the Company and of HongkongBank in 1991.

*N R Knox
Age 66. Chairman of Marine Midland Banks, Inc. Appointed a non-executive Director of the Company in 1990. A non-executive Director of HongkongBank from 1988 to 1992.

*C D Mackay
Age 54. Deputy Chairman and Chief Executive of Inchcape plc. A non-executive Director of British Airways Plc. Appointed a non-executive Director in 1990. A non-executive Director of HongkongBank from 1986 to 1992 and of Midland Bank plc from 1992 to 1993.

*G Maitland Smith
Age 62. Chairman of Sears plc. A Director of Midland Bank plc since 1986 and non-executive Deputy Chairman since 1992; non-executive Chairman of Hammerson plc. Appointed a non-executive Director in 1993.

*Sir Colin Marshall
Age 61. Chairman of British Airways Plc. A Director of USAir Group Inc., Qantas Airways Limited, IBM United Kingdom Holdings Limited and British Telecommunications plc. A member of the Board of the New York Stock Exchange. Appointed a non-executive Director in 1993. A non-executive Director of Midland Bank plc from 1989 to 1994.

*M Murofushi
Age 63. President and Chief Executive Officer of ITOCHU Corporation. Special Adviser and Chairman of the Policy, Planning and Foundation Committee of the Japan Chamber of Commerce and Industry and of the Committee on Corporate Laws and Regulations of the Keizai Doyukai (Japan Association of Corporate Executives). A member of the Executive Committee of the Trilateral Commission. Appointed a non-executive Director in 1992.

*Sir Wilfrid Newton, CBE
Age 66. Chairman of Raglan Properties plc, John I. Jacobs PLC and Mountcity Holdings Limited. A non-executive Director of Maunsell Holdings Limited and Sketchley plc. Appointed a non-executive Director in 1990. A non-executive Director of Midland Bank plc since 1992. Former Chairman of Mass Transit Railway Corporation and of London Regional Transport and a non-executive Director of HongkongBank from 1986 to 1992.

*H Sohmen, OBE
Age 55. Chairman of World-Wide Shipping Agency Limited, World-Wide Shipping Group Limited, World Maritime Limited, World Shipping and Investment Company Limited and World Finance International Limited and a Director of Nordström & Thulin AB. A non-executive Director of HongkongBank since 1984. Appointed a non-executive Director of the Company in 1990.

J E Strickland
Age 55. Executive Director Services. Appointed a Director in 1988. Joined HongkongBank in 1971 (previous service 1966-69); appointed an executive Director in 1989. Chairman of Wayfoong Property Limited and a Director of Marine Midland Bank and Midland Bank plc.

*Sir Adrian Swire
Age 63. Chairman of John Swire & Sons Limited and a Director of Swire Pacific Limited and Cathay Pacific Airways Limited. A member of the General Committee of Lloyd's Register of Shipping. Former Chairman of the International Chamber of Shipping and former President of the General Council of British Shipping. Appointed a non-executive Director in February 1995.

K R Whitson
Age 51. Appointed a Director in April 1994; a Director since 1992 and Chief Executive since April 1994 of Midland Bank plc; Chairman of Midland Life Limited and Forward Trust Group Limited and Deputy Chairman of the Supervisory Board of Trinkaus und Burkhardt KGaA.

* *Independent non-executive Directors*

Secretary

R G Barber
Age 44. Group Company Secretary. Joined HongkongBank as Assistant Secretary in 1980; Corporation Secretary from 1986 to 1992. Appointed Secretary of HSBC Holdings plc in 1990 and Secretary of Midland Bank plc in 1994.

Board of Directors and Group General Managers *(continued)*

Advisers to the Board

F R Frame
Age 65. Former Deputy Chairman of HongkongBank. Chairman of Wallem Group Limited and a non-executive Director of Baxter International Inc and Edinburgh Dragon Trust plc.

Sir Quo-Wei Lee, CBE
Age 76. Chairman of Hang Seng Bank Limited and Deputy Chairman of Hysan Development Company Limited. A Director of Miramar Hotel and Investment Company Limited, Furama Hotel Enterprises Limited, New World Development Company Limited, Shaw Brothers (Hong Kong) Limited and The Kowloon Motor Bus Company (1933) Limited. Chairman and Life Member of the Council of The Chinese University of Hong Kong. A member of the Governor's Business Council and Exchange Fund Advisory Committee and a Hong Kong Affairs Adviser appointed by the Chinese Government. A non-executive Director of HongkongBank from 1978 to 1984.

Group General Managers

D Beath
Age 56. General Manager and Group Audit Controller. Joined HongkongBank in 1960. Appointed General Manager in 1993.

C Carr
Age 57. General Manager and Group Legal Adviser. Joined HongkongBank in 1989 as a General Manager.

J H Cleave
Age 52. President and Chief Executive Officer of Marine Midland Bank. Joined Hongkong Bank of Canada in 1981; appointed President and Chief Executive Officer in 1987 and became a General Manager in 1991, prior to moving to his current role in 1992.

W R P Dalton
Age 51. President and Chief Executive Officer of Hongkong Bank of Canada. Joined Hongkong Bank of Canada in 1981; appointed to his current role in 1992 and became a General Manager in 1994.

A Dixon
Age 50. A General Manager of HongkongBank. Joined HongkongBank in 1965; appointed to his current role in February 1995. Previously Managing Director of The Saudi British Bank.

D G Eldon
Age 49. Executive Director of HongkongBank. Joined HongkongBank in 1968; appointed to his current role in 1994. Previously General Manager and Chief Executive Officer Malaysia.

F J French
Age 56. Group General Manager Credit and Risk. Joined HongkongBank in 1959; appointed to his current role in 1992.

S K Green
Age 46. General Manager and Group Treasurer. Joined HongkongBank in 1982; appointed to his current role in 1993, having been Group Treasurer since 1992.

C P Langley
Age 50. Chief Executive Officer Malaysia, Hongkong Bank Malaysia Berhad. Joined HongkongBank in 1961; appointed a General Manager in 1993.

A Mehta
Age 48. Chairman and Chief Executive of HSBC Holdings Inc. Joined HongkongBank in 1968; appointed a General Manager in 1991.

T W O'Brien
Age 47. Group General Manager Private Banking and Trustee. Joined HongkongBank in 1969; appointed a General Manager of HongkongBank in 1991. Previously General Manager and Chief Executive Officer UK of HongkongBank.

R M J Orgill
Age 56. Deputy Chief Executive of Midland Bank plc. Joined HongkongBank in 1958. Previously General Manager and Chief Executive Officer Malaysia.

J C S Rankin
Age 53. A General Manager of HongkongBank. Joined HongkongBank in 1960; appointed a General Manager of HongkongBank in 1990. Previously General Manager Group Human Resources.

P E Selway-Swift
Age 50. Executive Director Hong Kong and China of HongkongBank. Joined HongkongBank in 1962; appointed a General Manager of HongkongBank in 1988.

R A Tennant
Age 52. General Manager Group Human Resources. Joined Midland Bank plc in 1960 and HongkongBank in 1991. Appointed a General Manager in 1993.

Report of the Directors

Results for 1994

The Group profit for the year attributable to shareholders of the Company was £2,053 million, an increase of 14 per cent.

The Directors recommend the payment of a final dividend of 19p per ordinary share on 30 May 1995 to shareholders who are registered at the close of business on 13 April 1995. With the interim dividend of 8p per ordinary share paid on 18 November 1994, the total distribution for the year will amount to £703 million. The dividend will be payable in cash, in sterling or in Hong Kong dollars at an exchange rate to be fixed on 15 May 1995, with a scrip dividend alternative. The reserves available for distribution before accounting for the final dividend of £495 million are £3,425 million.

Further information about the results is given in the accompanying consolidated profit and loss account on page 43.

Principal Activities and Business Review

Through its subsidiary and associated undertakings, the Group provides a comprehensive range of banking and related financial services through an international network of more than 3,000 offices in 68 countries in the Asia-Pacific region, Europe, the Middle East and the Americas.

A review of the development of the business of Group undertakings during the year, particulars of important events since the end of the year and an indication of likely future developments are given in the 'Review of the Group' on pages 8 to 19.

Taken together, the five largest customers of the Group do not account for more than 1 per cent of the Group's income.

Capital and Reserves

The following events occurred during the year:

1. 26,006,387 ordinary shares of 75p and 43,078,299 ordinary shares of HK$10 each were issued on 10 June 1994 at par in lieu of the 1993 final dividend to shareholders who elected to receive new shares in lieu of cash dividends under the enhanced scrip dividend alternative. Shareholders' entitlements to new shares were calculated by reference to the average market price per share of 728.87636p and to the cash dividend enhanced by 50 per cent.

2. 441,661 ordinary shares of 75p and 4,268,347 ordinary shares of HK$10 each were issued on 18 November 1994 at par in lieu of the 1994 interim dividend to shareholders who elected to receive new shares in lieu of cash dividends. The average market price per share used to calculate shareholders' entitlements to new shares was 765p.

3. Options over 1,093,250 ordinary shares of 75p each were granted at nil consideration on 8 March 1994 and options over 65,000 ordinary shares of 75p each were granted on 23 August 1994, also at nil consideration, under the Company's executive share option scheme. The options were granted at the market value at the date of the grant. Options outstanding under this scheme on 1 June 1994 were increased by 9,815 and the exercise prices adjusted for the bonus element of the enhanced scrip alternative to the 1993 final dividend in accordance with the terms of the scheme. These options are exercisable between the third and tenth anniversaries of the grant at adjusted prices of 851.27p and 722.40p per share, respectively.

4. Options over 10,204,211 ordinary shares of 75p each were granted at nil consideration on 11 April 1994 to UK resident employees under the Company's savings-related share option scheme. The options were granted at 15 per cent discount to market value at the date of the grant. Options outstanding under this scheme on 1 June 1994 were increased by 80,008 and the exercise prices adjusted for the bonus element of the enhanced scrip alternative to the 1993 final dividend in accordance with the terms of the scheme. These options are exercisable within the period of six months commencing on the fifth anniversary of the relevant savings contract at an adjusted price of 700.84p per share.

5. Options over 7,795,280 ordinary shares of 75p each were granted at nil consideration on 26 September 1994 to Group employees resident in more than 40 overseas countries under the Company's savings-related share option scheme. These options were granted at 15 per cent discount to market value at the date of the grant and are exercisable within the period of six months commencing on the fifth anniversary of the relevant savings contract at a price of 610.47p per share.
6. Options over 768 ordinary shares of 75p each were exercised at a price of 700.84p per share under the Company's savings-related share option scheme and options over 412,590 shares lapsed.
7. No options under the Company's executive share option scheme were exercised during the year and options over 16,882 ordinary shares of 75p each lapsed.
8. Options under the Midland Bank employee savings-related and executive share option schemes were exercised over 3,849,134 ordinary shares of 75p each of the Company at prices ranging from 118.43p to 238.47p and options over 388,509 shares lapsed. Options outstanding under these schemes on 1 June 1994 were increased by 174,914 and the exercise prices adjusted for the bonus element of the enhanced scrip alternative to the 1993 final dividend in accordance with the terms of the schemes.

Annual General Meeting

The Annual General Meeting of the Company will be held at the Barbican Hall, Barbican Centre, London EC2 on Friday, 26 May 1995, at 11.00 a.m.

Close Company Provisions

The close company provisions of the Income and Corporation Taxes Act 1988 do not apply to the Company.

Valuation of Freehold and Leasehold Land and Buildings

The market value of the Group's properties has been reassessed by the Group's professional valuation staff and it is estimated that overall there was a surplus of approximately £1.5 billion over the value at which they are included in the consolidated balance sheet. The Group's properties are subject to a comprehensive valuation on a triennial basis for the purpose of updating the balance sheet value. The next such valuation will be made as at 31 December 1995.

Directors

The names of the Directors of the Company serving at the date of this Report and brief biographical notes are set out on page 23.

In 1994, Sir Brian Pearse retired as a Director of the Company and K R Whitson, who succeeded Sir Brian as Chief Executive of Midland Bank, was appointed an executive Director of the Company.

D P H Liao retired as a Director of the Company on 24 February 1995. On the same date, Sir Adrian Swire was appointed a non-executive Director of the Company. Having been appointed since the last Annual General Meeting, he will retire at the forthcoming Annual General Meeting and, being eligible, offers himself for re-election.

B H Asher, Baroness Dunn, Sir Joseph Hotung, C D Mackay, Sir William Purves and J E Strickland will retire by rotation at the Annual General Meeting and, being eligible, offer themselves for re-election.

None of the Directors proposed for re-election at the Annual General Meeting has a service contract with the Company or a subsidiary undertaking of the Company which is not determinable within one year without payment of compensation.

Directors' Interests

According to the registers of Directors' interests kept by the Company under Section 325 of the Companies Act 1985 and Section 29 of the Securities (Disclosure of Interests) Ordinance, the Directors of the Company at the year-end had the following interests, all beneficial, in the shares and loan capital of the Company:

	At 1 January 1994 (or at date of appointment if later)	*At 31 December 1994* Personal	Family	Corporate	Other	Total
Ordinary Shares of HK$10						
B H Asher	2,100	2,100	—	—	—	2,100
J R H Bond	15,830	16,538	—	—	—	16,538
D E Connolly	178,235	186,214	—	—	—	186,214
J M Gray	16,571	3,836	13,470	—	—	17,306
Sir Joseph Hotung	520,249	249	—	654,439*	—	654,688
N R Knox	7,560	7,810	—	—	—	7,810
D P H Liao	17,669	22,500	—	—	—	22,500
Sir Wilfrid Newton	3,356	3,505	—	—	—	3,505
Sir William Purves	40,861	34,331	—	—	—	34,331
H Sohmen	651,671	—	165,567	590,379*	—	755,946
J E Strickland	26,868	27,129	939	—	—	28,068
K R Whitson	1,524	1,591	—	—	—	1,591
Ordinary Shares of 75p						
R Delbridge	7,372	7,621	—	—	—	7,621
D P H Liao	7,008	7,320	—	—	—	7,320
C D Mackay	—	7,500	—	—	—	7,500
G Maitland Smith	1,742	1,805	—	—	—	1,805
Sir Colin Marshall	1,842	1,923	—	—	—	1,923
Sir Wilfrid Newton	—	2,000	—	—	—	2,000
Sir William Purves	1,311	1,369	—	—	—	1,369
Sir Peter Walters	12,578	13,005	—	—	—	13,005
11.69% Subordinated Bonds 2002 (£)						
J R H Bond	500,000	500,000	—	—	—	500,000
R Delbridge	3,900	3,900	—	—	—	3,900
Baroness Dunn	70,000	70,000	—	—	—	70,000
D P H Liao	3,622	3,622	—	—	—	3,622
G Maitland Smith	910	910	—	—	—	910
Sir Colin Marshall	975	975	—	—	—	975
Sir Wilfrid Newton	35,000	35,000	—	—	—	35,000
Sir Peter Walters	6,500	6,500	—	—	—	6,500
Subordinated Collared Floating Rate Notes 2008 (US$)						
Sir Joseph Hotung	1,000,000	—	—	—	—	—

**Interests held by private investment companies*

At 31 December 1994, the undernamed Directors held options to acquire the number of HSBC Holdings plc ordinary shares of 75p each set against their respective names. The options were granted for nil consideration at exercise prices equivalent to the market value at the date of grant, except that options granted under the Company's savings-related share option scheme were granted at 15 per cent discount to market value, and options granted under the Midland Bank savings-related share option scheme were granted at 20 per cent discount. The number of shares and the exercise prices of options outstanding on 1 June 1994 were adjusted in accordance with the terms of the share option schemes for the bonus element of the enhanced scrip alternative to the 1993 final dividend. There are no performance criteria conditional upon which the options are exercisable. No options granted to Directors lapsed during the year. The market value of the ordinary shares of 75p each at 30 December 1994 (the last day in 1994 when the London Stock Exchange was open for business) was 706p. The highest and lowest market values during the year were 1,099p and 661p. Market value is the mid-market price quoted on the London Stock Exchange on the relevant date.

	Options held at 1 January 1994 (or at date of appointment if later)	*Options granted during year*	*Options exercised during year*	*Options held at 31 December 1994*	*Exercise price in pence*	*Exercisable from*	*Exercisable until*
B H Asher	12,500		—	12,613*	721.84	12 Oct 1996	12 Oct 2003
		15,000	—	15,136*	851.27	8 Mar 1997	8 Mar 2004
J R H Bond	20,000		—	20,181*	721.84	12 Oct 1996	12 Oct 2003
		20,000	—	20,181*	851.27	8 Mar 1997	8 Mar 2004
R Delbridge	3,312		—	3,342*†	118.43	1 Jul 1996	31 Dec 1996
	10,000		—	10,090*	721.84	12 Oct 1996	12 Oct 2003
		15,000	—	15,136*	851.27	8 Mar 1997	8 Mar 2004
		1,463	—	1,476*‡	700.84	1 Jul 1999	31 Dec 1999
J M Gray	15,000		—	15,136*	721.84	12 Oct 1996	12 Oct 2003
		25,000	—	25,227*	851.27	8 Mar 1997	8 Mar 2004
		1,695	—	1,695‡	610.47	1 Dec 1999	31 May 2000
Sir William Purves	25,000		—	25,227*	721.84	12 Oct 1996	12 Oct 2003
		45,000	—	45,408*	851.27	8 Mar 1997	8 Mar 2004
		1,463	—	1,476*‡	700.84	1 Jul 1999	31 Dec 1999
J E Strickland	10,000		—	10,090*	721.84	12 Oct 1996	12 Oct 2003
		15,000	—	15,136*	851.27	8 Mar 1997	8 Mar 2004
K R Whitson	8,500		—	8,577*	721.84	12 Oct 1996	12 Oct 2003
		12,500¶	—	12,613*	851.27	8 Mar 1997	8 Mar 2004

* *Adjusted for the bonus element of the enhanced scrip alternative to the 1993 final dividend*
† *Options granted under the Midland Bank savings-related share option scheme*
‡ *Options granted under the Company's savings-related share option scheme*
¶ *Held at date of appointment, 1 April 1994*

Sir Joseph Hotung has a personal interest in HK$10 million of The Hongkong and Shanghai Banking Corporation Limited Subordinated Collared Floating Rate Notes 2003, which he held at the beginning of the year and at the end of the year.

On 21 March 1994, J R H Bond, N R Knox and Sir William Purves each ceased to have a personal interest in 10 shares of common stock of Marine Midland Bank which they had held as directors of that company at the beginning of the year.

Save as stated above, none of the Directors had an interest in any shares or debentures of any Group company at 1 January 1994 or at 31 December 1994 and none of the Directors, or members of their immediate families, was granted or exercised any right to subscribe for any shares or debentures during the year.

There have been no changes in these interests since 31 December 1994.

None of the Directors had during or at the end of the year a material interest, directly or indirectly, in any contract of significance with the Company or any of its subsidiary undertakings.

Directors' Emoluments

The emoluments of the Directors of the Company for 1994 were as follows:

	Fees £000	Salary and other remuneration £000	Benefits in kind £000	Discretionary bonuses[6] £000	Pension contributions £000	Total £000
Executive Directors						
Sir William Purves	15	484	34	100	—	633
— waived	(13)					(13)
J M Gray[1]	13	366	436	—	65	880
— waived	(15)					(15)
J R H Bond	15	400	20	130	54	619
— waived	(13)					(13)
B H Asher	15	370	7	130	—	522
R Delbridge	15	324	4	30	25	398
J E Strickland	15	288	24	30	—	357
— waived	(13)					(13)
K R Whitson[2]	11	219	17	45	28	320
Sir Brian Pearse[3]	4	80	6	—	—	90
Non-executive Directors						
Sir Peter Walters[4]	15	52	—	—	—	67
G Maitland Smith[5]	15	49	—	—	—	64
N R Knox	60	—	—	—	—	60
Sir Wilfrid Newton	30	5	—	—	—	35
D E Connolly	28	3	—	—	—	31
Sir Joseph Hotung	28	3	—	—	—	31
Baroness Dunn	28	2	—	—	—	30
D P H Liao	28	—	—	—	—	28
Sir Colin Marshall	19	—	—	—	—	19
H Sohmen	13	3	—	—	—	16
— waived	(15)	(2)				(17)
C D Mackay	15	—	—	—	—	15
M Murofushi	15	—	—	—	—	15
Total	397	2,648	548	465	172	4,230

1 The emoluments of J M Gray include housing and other expatriate benefits in kind which are normal within the location in which he is employed.
2 Appointed on 1 April 1994.
3 Resigned on 31 March 1994.
4 As Chairman of Midland Bank plc until 31 March 1994, Sir Peter Walters received a salary of £50,000 which is included above.
5 As Deputy Chairman of Midland Bank plc, G Maitland Smith received a salary of £40,000 which is included above.
6 These discretionary bonuses in respect of 1994 will be paid in 1995.

Pensions

The pension provision for J M Gray is covered under the International Staff Retirement Benefits Scheme of The Hongkong and Shanghai Banking Corporation Limited.

For J R H Bond and K R Whitson, pension arrangements to contractual retirement age of 60 are provided under The HongkongBank Group London Staff Pension Fund.

For R Delbridge, pension arrangements to contractual retirement age of 60 are provided under the Midland Bank and Midland Bank Executive schemes. In addition, provision is made, by way of an unfunded commitment, to ensure a pension of two-thirds of final salary. The charge to the profit and loss account in respect of this was £122,000 in 1994.

Report of the Directors *(continued)*

Employees' Emoluments

Set out below is information in respect of the five employees, other than Directors of the Company, whose emoluments (excluding commissions or bonuses related to the revenue or profits generated by the employees individually or collectively with others engaged in similar activities) were the highest in the Group for the year ended 31 December 1994.

	£000
Basic salaries, allowances and benefits in kind	1,259
Bonuses paid or receivable	1,324
Pension contributions	182
Amounts paid as inducements to join or on joining the Group	60
Compensation for loss of office	550
	3,375

Their emoluments are within the following bands:

	Number of employees
£600,001 – £650,000	2
£650,001 – £700,000	1
£700,001 – £750,000	2

Directors' and Officers' Liability Insurance

Directors' and officers' liability insurance was maintained during the year.

Employee Involvement

The Company regards communication with its employees as a key aspect of its policies. Information is given to employees about employment matters and the financial and economic factors affecting the Group's performance, through management channels, in-house magazines and attendance at internal seminars and training programmes. Employees are encouraged to discuss operational and strategic issues with their line management and to make suggestions to improve operational performance. The involvement of employees in the performance of the Group is further encouraged through participation in bonus and share option schemes as appropriate.

About 29,000 Group employees in the UK and in more than 40 other countries joined the Company's savings-related share option scheme which was launched in 1994.

Employment of Disabled Persons

The Company is committed to providing equal opportunities in employment. The employment of disabled persons is included in this commitment and the recruitment, training, career development and promotion of disabled persons are based on the aptitudes and abilities of the individual. Should employees become disabled during employment, every effort would be made to continue their employment and, if necessary, appropriate training would be provided.

Substantial Interests in Share Capital

The following interests in the Company's ordinary shares of 75p each are recorded in the register maintained under Section 211 of the Companies Act 1985:

The Prudential Corporation Group of Companies	4.20 per cent
Standard Life Group	3.45 per cent
Legal & General Group	3.37 per cent

No substantial interest in any of the equity share capital is recorded in the register maintained by the Company under Section 161(1) of the Securities (Disclosure of Interests) Ordinance.

Dealings in HSBC Holdings plc Shares

During the year, subsidiary undertakings of the Company sold on The Stock Exchange of Hong Kong a total of 336,000 ordinary shares of HK$10 each. The aggregate consideration for the sales was £2,691,000.

James Capel & Co. Limited is a market maker in London in the shares of the Company.

Donations

During the year, the Group made charitable donations totalling £4,420,000. Of this amount £1,804,000 was given for charitable purposes in the United Kingdom. No political donations were made in 1994.

Corporate Governance

The Company has complied throughout the year with the operative provisions of the Code of Best Practice contained in the Report of the Committee on the Financial Aspects of Corporate Governance ('the Cadbury Committee') published in December 1992. The provisions of the Code under which directors are required to report on their company's systems of internal control will come into effect in respect of the *Annual Report and Accounts* for 1995, following publication of guidance for directors as recommended in the Cadbury Committee's report.

The Board has appointed a number of committees consisting of certain Directors and senior executives. The following are the principal committees:

Group Executive Committee

The Group Executive Committee meets regularly and operates as a general management committee under the direct authority of the Board. The members of the Committee at the date of this report are J R H Bond (Chairman), B H Asher, R Delbridge, J M Gray, Sir William Purves, J E Strickland and K R Whitson, Directors, and F J French, S K Green and A Mehta, Group General Managers.

Group Audit Committee

The Group Audit Committee meets regularly with the Group's senior financial, internal audit and compliance management and the external auditors to consider the nature and scope of audit reviews and the effectiveness of the systems of internal control and compliance. The members of the Group Audit Committee are Sir Wilfrid Newton (Chairman), D E Connolly and G Maitland Smith, all of whom are non-executive Directors, and F R Frame, Adviser to the Board.

Remuneration Committee

The Remuneration Committee meets regularly to consider human resource policies of the Group, particularly those governing terms and conditions of employment, remuneration, retirement benefits, development of high potential employees and key succession planning, and to make recommendations to the Board. The members of the Remuneration Committee are Baroness Dunn (Chairman), H Sohmen and Sir Peter Walters, all of whom are non-executive Directors, and R A Tennant, General Manager Group Human Resources.

Nomination Committee

This Committee carries out the process of nominating candidates to fill vacancies on the Board of Directors. The members of the Committee are the members of the Remuneration Committee together with the Group Chairman.

Auditors

Consequent upon the transfer of the Head Office of the Company to London on 1 January 1993, KPMG Peat Marwick of Hong Kong retired at the 1993 Annual General Meeting and KPMG Peat Marwick of London, their associated firm, were appointed in their place.

On 6 February 1995, KPMG Peat Marwick changed the name under which they practise to KPMG and, accordingly, have signed their report in their new name.

KPMG have expressed their willingness to continue in office. A resolution proposing their reappointment and giving authority to the Directors to fix their remuneration will be submitted to the forthcoming Annual General Meeting.

On behalf of the Board
R G Barber, *Secretary*

27 February 1995

Summary of Financial Performance

Group profit

The HSBC Group made a profit before tax of £3,166 million in 1994, an increase of £582 million, or 23 per cent, over 1993. In Hong Kong dollar terms, pre-tax profit grew by 27 per cent from HK$29,509 million to HK$37,527 million. There was a decline in operating income of £390 million from 1993, as a result of lower dealing profits, particularly in interest rate related trading, with the very favourable market conditions in 1993 not being repeated in 1994. Other sources of operating income continued to improve.

The Group's charges for doubtful debts were £883 million lower than 1993. Lower charges in Midland, HongkongBank and Concord Leasing were partially offset by reduced write-backs of provisions made in prior years in Marine Midland Bank.

Profit attributable to shareholders increased from £1,806 million (HK$20,624 million) in 1993 to £2,053 million (HK$24,334 million), an increase in sterling terms of 14 per cent (18 per cent in Hong Kong dollars). At constant exchange rates, the increase in attributable profit over 1993 was £283 million, or 16 per cent.

The results of overseas branches and subsidiary and associated undertakings are translated into sterling at the average rate of exchange for the year. Previously, these results were translated at the year-end exchange rate. The 1994 profit attributable to shareholders increased by £29 million as a result of this change.

Shareholder ratios

Earnings per share increased by 12 per cent, from 71.1 pence to 79.6 pence.

The headline earnings per share, which is calculated in accordance with the Institute of Investment Management and Research Statement of Investment Practice, also increased by 12 per cent to 76.8 pence. The headline earnings per share excludes profits on the sale of tangible fixed assets; on the disposal of a subsidiary, Euromobiliare; and on the part disposal of the investment in the 3i Group in 1994, and of a subsidiary, Wing On Bank, in 1993.

Return on average shareholders' funds at 20.4 per cent, was reduced slightly from 20.8 per cent in 1993.

Shareholders' funds rose by £1,456 million to £10,790 million, following the retention of £1,350 million of Group profits, additional capital of £372 million arising from scrip dividends and a surplus on investment properties of £125 million.

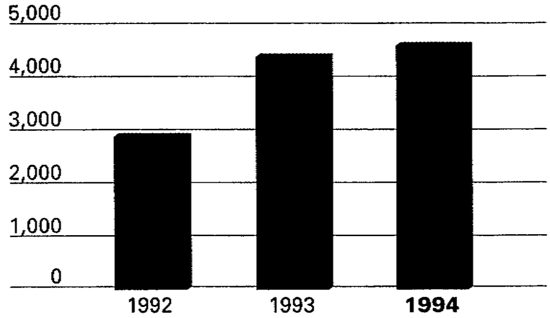
The Directors have recommended a final dividend of 19 pence per share. Together with the interim dividend of 8 pence, the total dividend for the year amounts to 27 pence (1993: 23.5 pence), an increase of 15 per cent. The dividend is covered 2.9 times by attributable profit (1993: 3 times).

Net interest income

Net interest income rose by £159 million to £4,597 million, mainly from an underlying increase in average interest-earning assets. There was a slight improvement in the interest margin (calculated as net interest income divided by average interest-earning assets). A recovery of £76 million arising from sales of less developed country (LDC) interest was included in 1994 (1993: £87 million).

Action by Midland to formalise netting arrangements with customers led to a reduction in average interest-earning assets of £3.2 billion in 1994 over 1993. After allowing for this, the underlying growth in average interest-earning assets was £4.0 billion, or 2.4 per cent, in 1994. The underlying growth occurred mainly in loans and advances to customers (£2.7 billion higher) and money market accounts (£1.4 billion higher). The increase in customer loans and advances relates mainly to the HongkongBank Group which continued to experience strong demand, particularly in Hong Kong.

Net interest income (£m)

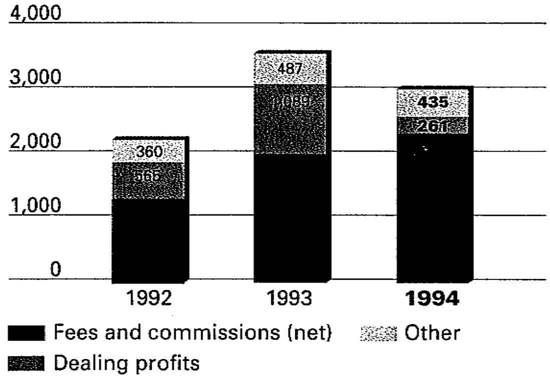


The Group's net interest margin for 1994 improved slightly from 2.67 per cent in 1993 to 2.71 per cent, after allowing for the effect of netting of loans and deposits. This reflects sustained margins in most of the Group's principal areas of operation. In Midland, the benefit of an increase in net free funds was offset by a reduction in the spread between rates paid for deposits and yields on assets and the effect of lower interest rates. In the HongkongBank Group, margins remained broadly at the same level as in 1993 while average interest-earning assets increased by 8.2 per cent (excluding Malaysia). Higher interest earned on free funds was offset by a narrowing in the net interest spread in Hong Kong.

Non-interest income

There was a decrease in non-interest income of £549 million (15 per cent) to £3,027 million.

Non-interest income (£m)



Dealing profits were £261 million, £828 million or 76 per cent lower than 1993. The decrease was mainly in interest rate derivatives and securities trading in Midland and HongkongBank in Hong Kong. Dealing profits included foreign exchange income of £343 million, compared with £377 million in 1993. Proprietary position taking in both interest rate derivatives and securities lost £93 million in 1994 compared with a profit of £199 million in 1993.

Dealing in securities resulted in a loss of £31 million in 1994, including the interest spread on dealing assets, compared with a profit of £383 million in 1993.

The term 'dealing profits' is a prescribed heading under the UK implementation of the European Union Bank Accounts Directive; it excludes net interest income, fees and commissions, and the cost of associated staff and other administrative expenses. The table below shows the net interest income attributable to dealing activities. The net interest income on securities trading arises on marked-to-market debt securities and treasury bills.

Fee, commission and other income at £2,939 million, improved by £132 million compared with 1993. Fee and commission income in the UK was £89 million higher than 1993, most of which was reported by investment banking and Midland. Midland branch fee and commission income reduced following pricing revisions for personal customers in mid-1993. However, this decrease was partly offset by increased fee income from card services and mortgages. Other areas showing fee increases include First Direct and asset finance. The continued growth in customer demand for corporate and retail services contributed to a £34 million rise in Hong Kong.

Fees and commissions payable at £173 million, were £147 million lower than 1993 mainly due to a reduction in the amortisation of mortgage servicing rights in Marine Midland of £145 million.

	1994			1993		
Analysis of income from dealing in financial instruments (£m)	Dealing profits	Net interest income (expense)	Total	Dealing profits	Net interest income (expense)	Total
Foreign exchange	**343**	**7**	**350**	377	(2)	375
Interest rate derivatives	**2**	**(1)**	**1**	335	(13)	322
Securities	**(111)**	**80**	**(31)**	290	93	383
Equities and other trading	**27**	**6**	**33**	87	1	88
	261	**92**	**353**	1,089	79	1,168

Operating expenses

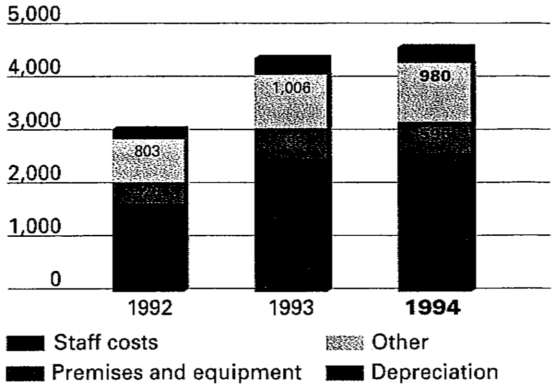
Staff costs were up by £144 million, or 6 per cent, compared with 1993. At constant exchange rates, the increase was £175 million, or 7 per cent. Midland has recruited additional staff to service growth in First Direct, Midland Personal Financial Services and mortgages. This increase in staff numbers and the 1994 pay award, together with a £13 million charge for additional pension contributions following the 1993 actuarial valuation of the Midland Bank Pension Scheme, caused Midland's staff costs on continuing operations to rise by £67 million. HongkongBank staff costs rose by £45 million, reflecting an increase in staff numbers, mainly in Hong Kong, and pay rises in line with local inflation rates.

Premises and equipment costs (which now include property taxes, repairs and maintenance and expenditure on utilities as well as rental costs) were flat compared with 1993.

The charge for depreciation increased by £22 million, or 7 per cent, mainly as a result of the depreciation of operating lease assets in Midland which acquired Swan National Leasing in July 1993.

The cost:income ratio rose from 55.2 per cent in 1993 to 59.9 per cent, and resulted from a decrease in total operating income of 5 per cent, while operating expenses rose by 3 per cent.

Operating expenses (£m)



	Full-time equivalent		
Staff numbers	**1994**	1993	1992
HongkongBank	**21,877**	24,403	23,468
Hang Seng Bank	**7,499**	6,995	7,234
Midland Bank	**45,900**	45,088	46,008
Marine Midland Bank	**8,213**	8,409	9,105
Hongkong Bank of Canada	**3,100**	2,943	2,536
The British Bank of the Middle East	**2,333**	2,240	2,120
Hongkong Bank Malaysia	**3,861**	0*	0*
Other	**8,954**	8,688	8, 245
Total	**101,737**	98,766	98,716

** Hongkong Bank Malaysia's branch staff numbers were included in HongkongBank in 1992 and 1993.*

Bad and doubtful debts

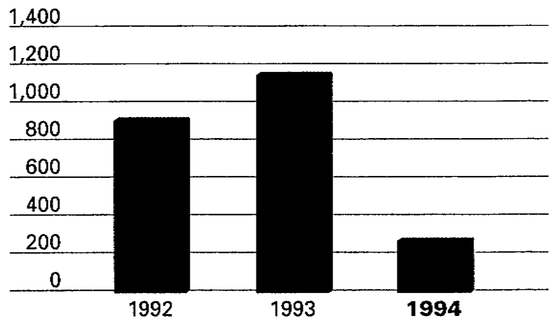
The £275 million charge against profit for the year was £883 million below 1993. While new provisions raised, at £893 million, were £675 million lower than 1993, £494 million of provisions were released and £124 million of provisions previously written off were recovered.

The charge in Midland Bank of £98 million was £572 million lower than in 1993. There were sharp reductions in both the domestic UK charge, which was £338 million lower at £164 million, and in the international charge (excluding LDCs), which was £130 million lower at £1 million. In addition, Midland reported a net release of £67 million relating to LDC loans, mainly as a result of sales of debt, compared with a charge of £37 million in 1993.

Concord Leasing recorded a charge of £111 million as additional provisions were required, mainly against the aviation portfolio. The charge made in 1993 was £160 million.

There was a net recovery in the HongkongBank Group of £6 million, compared with a charge of £295 million in 1993, reflecting a continued general improvement in the credit quality of the loan book.

Charge for bad and doubtful debts (£m)



Profit on disposal of fixed assets and investments

The Group's profits on disposal of fixed assets and investments increased by £79 million to £366 million.

Hang Seng Bank recorded profits in 1994 of £186 million (£159 million in 1993), mainly from the sale of listed equity investments and bonds. A profit of £64 million arose from the disposal of part of Midland's shareholding in the 3i Group. Most of the other profits arose from the sale of venture capital investments.

There continues to be a substantial unrecognised surplus on equities held for investment purposes of £531 million (1993: £1,023 million). The reduction during the year resulted from both the sale of equities by Hang Seng Bank and the decline in the Hong Kong stock-market.

Investments in debt securities at 31 December 1994 have unrecognised losses of £151 million, net of gains on hedge contracts (1993: net unrecognised gains of £64 million).

Taxation

The 1994 effective rate of tax was 26.2 per cent compared with 19.9 per cent in 1993. The effective tax rate was lower in 1993 because of the larger availability of previously unrecognised credits in respect of tax losses, particularly in the UK and USA. However, the level of current year unrelieved trading losses was lower in 1994.

The effective rate of tax was below the standard 33 per cent rate of UK corporation tax, mainly because of lower rates of tax in major subsidiaries overseas (and for 1993 previously unrecognised tax losses). The benefit of these lower rates of tax was partially offset by unrelieved losses overseas, particularly in the USA.

Analysis of overall tax charge (£m)	**1994**	1993
Taxation at UK corporation tax rate of 33 per cent	**1,045**	853
Net tax effect of differently taxed overseas profits	**(219)**	(206)
Unrelieved trading losses	**67**	113
Utilisation of previously unrecognised tax losses and advance corporation tax	**(52)**	(309)
Other items	**(12)**	64
	829	515

During the year, there was an advance corporation tax saving of £83 million as a result of an 80 per cent take-up on the enhanced scrip dividend alternative in respect of the 1993 final dividend paid during the year.

Assets

Total assets decreased by £6 billion compared with December 1993. At constant exchange rates assets increased by £600 million.

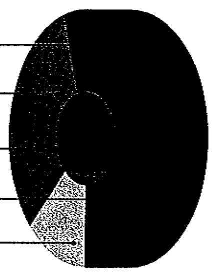
The relative proportion of assets within loans and advances to customers increased to 50.3 per cent of Group assets from 48.3 per cent at December 1993. Lending increased by £1.0 billion, or 1 per cent (3 per cent at constant exchange rates) during 1994. Loan demand remained strong in Asia, with HongkongBank reporting an overall increase of 11 per cent. Demand was particularly strong in Hong Kong where residential mortgage lending, corporate lending and trade finance remained buoyant. In the UK, customers' demand for lending remained subdued and growth in residential mortgages (particularly fixed rate mortgages) was partly offset by net repayments of other forms of personal lending and of lending to business customers.

Loans and advances to banks of £41.9 billion decreased by £3.8 billion, or 8 per cent, mainly due to reductions in Hong Kong, both by HongkongBank and Hang Seng Bank, reflecting a move from bank advances into treasury bills.

Debt securities decreased to 11 per cent of Group assets from 13 per cent at December 1993. Holdings of trading securities were reduced because of adverse market conditions for securities. Trading securities decreased by £4 billion and investment securities decreased by £1 billion.

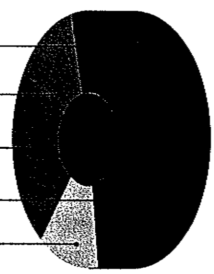
*Assets **1994** (excluding Hong Kong Government certificates of indebtedness)*

	%	£b
Treasury and other eligible bills	4.7	**9.3**
Debt securities	10.8	**21.3**
Loans and advances to banks	21.3	**41.9**
Loans and advances to customers	50.3	**98.8**
Other	12.9	**25.2**
Total	100.0	**196.5**



Assets 1993 (excluding Hong Kong Government certificates of indebtedness)

	%	£b
Treasury and other eligible bills	3.5	7.1
Debt securities	12.9	26.1
Loans and advances to banks	22.6	45.7
Loans and advances to customers	48.3	97.8
Other	12.7	25.6
Total	100.0	202.3



Capital Management

Capital measurement and allocation

Group capital adequacy is measured by the ratio of the Group's capital to risk-weighted assets, taking into account both balance sheet assets and off-balance-sheet transactions. Effective 1 January 1993, the Bank of England became the supervisor of the HSBC Group on a consolidated basis and, as such, receives information on the capital adequacy of, and sets capital requirements for, the Group as a whole. Individual banking subsidiaries are directly regulated by the appropriate local banking supervisors, which set and monitor capital adequacy requirements for them. Similarly, securities subsidiaries and other non-banking subsidiaries are subject to the supervision and capital requirements of relevant local authorities. Since 1988, when the governors of the Group of Ten central banks agreed to guidelines for the international convergence of capital measurement and standards, the banking supervisors of the Group's major banking subsidiaries have exercised capital adequacy supervision in a broadly similar framework. The Bank of England, in implementing the European Union Own Funds and Solvency Ratio Directives, requires each bank and banking group to maintain an individually prescribed ratio of total capital to risk-weighted assets.

It is the Group's policy to maintain a strong capital base to support development of the Group's business. It seeks to maintain a prudent balance between the different components of Group capital and, in the holding company, between the composition of its capital and that of its investment in subsidiaries.

Capital is divided into two tiers: tier 1, comprising shareholders' funds and minority interests, and tier 2, comprising general loan loss provisions, property revaluation reserves and qualifying subordinated loan capital. The amount of qualifying tier 2 capital cannot exceed that of tier 1 capital, and term subordinated loan capital may not exceed 50 per cent of tier 1 capital. There are also limitations on the amount of general provisions which may be included in tier 2 capital. Deductions in respect of intangible assets and unconsolidated investments are made from tier 1 capital and total capital, respectively.

Risk assets are measured by means of a hierarchy of risk weights classified according to the nature of each asset and counterparty. All off-balance-sheet items giving rise to credit, foreign exchange or interest rate risk are assigned weights appropriate to the category of the counterparty.

Group capital structure

During 1994, the Group's total capital ratio increased from 13.2 per cent to 14.4 per cent and its tier 1 capital ratio increased from 7.9 per cent to 9.1 per cent.

Tier 1 capital increased by £1,638 million (17 per cent) from the level at the end of 1993, mainly due to profit retentions of £1,350 million and an increase in minority interests of £211 million. Additional capital of £372 million arose from scrip dividends, of which £333 million related to the enhanced scrip dividend alternative offered to shareholders in respect of the 1993 final dividend. A reduction in reserves of £295 million arose from foreign currency translation adjustments and other reserves movements.

Tier 2 capital increased by £3 million. The appreciation of sterling against the US dollar reduced the amount of dollar denominated perpetual debt capital in sterling terms by £97 million. Additional term subordinated debt of US$400 million was issued by Midland Bank, which offset a £200 million reduction arising from exchange rate movements, repayments and regulatory amortisation of qualifying capital. Property revaluation reserves increased by £64 million, largely as a result of revaluation of investment properties held by subsidiaries.

Total risk-weighted assets increased by 1 per cent, although an increase of 4 per cent would have arisen at constant exchange rates.

£m	**1994**	1993
Composition of capital		
Tier 1:		
Shareholders' funds	**10,790**	9,334
Minority interests	**2,223**	2,012
Less: property revaluation reserve	**(1,478)**	(1,414)
Intangibles/Other	**(33)**	(68)
Total qualifying tier 1 capital	**11,502**	9,864
Tier 2:		
Property revaluation reserve	**1,478**	1,414
General provisions	**775**	789
Perpetual subordinated debt	**1,783**	1,880
Term subordinated debt	**3,190**	3,137
Minority interests		
(in tier 2 preference shares)	**63**	66
Total qualifying tier 2 capital	**7,289**	7,286
Unconsolidated investments	**(507)**	(563)
Investments in other banks	**(145)**	(49)
Other deductions	**(41)**	(28)
Total capital	**18,098**	16,510
Total risk-weighted assets	**125,823**	124,717
Capital ratios	**%**	%
Total capital/risk-weighted assets	**14.4**	13.2
Tier 1 capital/risk-weighted assets	**9.1**	7.9

Deployment of shareholders' funds

Shareholders' funds are deployed mainly in investment in its subsidiaries. At 31 December 1994, the major investments of shareholders' funds, compared with the previous year, were:

£m	1994	1993
Hang Seng Bank (61.48% owned)	1,808	1,794
HongkongBank and other subsidiaries	2,440	2,367
HongkongBank and subsidiaries	4,248	4,161
Midland Bank	2,702	2,506
Marine Midland Bank	894	862
Hongkong Bank Malaysia Berhad	257	—
Hongkong Bank of Canada	240	254
The British Bank of the Middle East	154	147
HSBC Investment Bank Limited	335	314*
Holding company and non-trading subsidiaries	1,204	536
Other subsidiaries	505	322
Consolidated associates	251	232
	10,790	9,334

** 1993 figure represents pro-forma consolidated shareholders' funds of HSBC Investment Banking Group Ltd, the previous holding company of the European investment banking businesses.*

It is Group policy for subsidiaries to retain sufficient profits to support planned business growth and to dividend any surplus profits to the holding company. During 1994, the effect of profit retentions for most overseas subsidiaries was reduced by foreign currency movements which resulted in relatively minor changes in the sterling level of subsidiaries' shareholders' funds.

The Malaysian branches of HongkongBank were transferred to Hongkong Bank Malaysia Berhad on 1 January 1994, and Hongkong Bank Malaysia Berhad was sold by HongkongBank to HSBC Holdings BV, a direct subsidiary of HSBC Holdings plc, on the same date.

HSBC Investment Bank Limited is a UK-based holding company and its consolidated shareholders' funds are substantially less than the sum of the share capital and reserves of all the subsidiaries included in the investment banking line of business (most notably due to HSBC Investment Bank Asia Holdings Limited being a subsidiary of HongkongBank).

The shareholders' funds of the holding company and non-trading subsidiaries represent the surplus of HSBC Holdings plc's equity capital over its equity investments, after adjusting for the capital structure of its immediate non-trading holding companies. The principal non-trading holding companies are HSBC Holdings (Investments) Limited, HSBC Holdings BV, and HSBC Holdings UK Limited. The equity resources of the holding company and non-trading subsidiaries increased by £668 million in 1994, reflecting the surplus of dividends from subsidiaries over new equity investments in subsidiaries and dividends to shareholders.

Credit Risk Management

Credit risk

Credit risk is the risk that a customer or counterparty of the Group will be unable or unwilling to meet a commitment that it has entered into with a member of the Group. It arises from the lending, trade finance, treasury and other activities undertaken by Group companies. The Group has in place policies and procedures for the control and monitoring of all such risks.

Group Head Office is responsible for the formulation of high-level credit policies; the independent review of the Group's largest credit exposures; the control of the Group's cross-border exposures; and portfolio management of risk concentrations. It also reviews the efficiency of Group companies' credit approval processes, a key element of which is the Group's universal facility grading system. The Group Executive Committee receives regular reports on credit exposures at both Group and subsidiary levels. These include information on asset concentrations, industry exposures, levels of bad debt provisioning and country exposure limits.

In each of the Group's subsidiaries, local management is responsible for the quality of its credit portfolios. Each subsidiary has established a credit process involving delegated approval authorities and credit procedures, the objective of which is to build and maintain risk assets of high quality.

The Group's credit risk limits to counterparties in the financial and government sectors are managed centrally to optimise the use of credit availability and to avoid excessive risk concentration. Group companies remain responsible for their own credit exposures. In addition to the portfolio management undertaken at Group level, each subsidiary manages its own risk concentrations on a market sector, geographical and product basis.

Cross-border risk is controlled through the imposition of country limits, with sub-limits by maturity and type of business. Transactions with higher risk countries are considered on a case-by-case basis.

Special attention is paid to the management of problem loans. Where deemed appropriate, specialist units are established to provide intensive management and control to maximise recoveries of doubtful debts.

Financial Review *(continued)*

Industry exposures

Loans and advances to customers are spread throughout the various industrial sectors, as well as geographically. Approximately one-third of loans and advances to customers are to the consumer sector and two-thirds are to commercial enterprises.

Residential mortgages now comprise 22.9 per cent of the overall portfolio, having increased by £2,032 million, or 9.5 per cent, during 1994. Much of the increase was due to net additional lending in the UK by Midland, whose mortgage book grew 16 per cent, as well as in Marine Midland, Hongkong Bank of Canada and Hang Seng Bank. Loan loss experience in this sector remains very good. Other consumer advances increased by 3.4 per cent during 1994, to £10,897 million.

Commercial, industrial and international trade loans decreased by £708 million, or 2.6 per cent, to £26,204 million. While demand remained buoyant in the Asia-Pacific region where increases in corporate lending and trade finance reflected continued economic growth, lending to Midland's business customers in the UK declined.

Real estate and construction advances increased by £1,122 million, or 7.6 per cent, to £15,821 million, mainly due to increased lending by HongkongBank and Hang Seng Bank in Hong Kong.

Advances to financial institutions other than banks decreased by £2,029 million, or 26.9 per cent. The majority of the decline resulted from the sale of Euromobiliare S.p.A.

Other advances decreased by £538 million, or 2.6 per cent, mainly due to lower settlement account balances.

Gross loans and advances to customers by industry exposure	**1994**		1993	
	£m	**%**	£m	%
Consumer:				
Residential mortgages	**23,450**	**22.9**	21,418	21.0
Other advances to individuals	**10,897**	**10.6**	10,543	10.3
Total consumer	**34,347**	**33.5**	31,961	31.3
Commercial:				
Commercial, industrial and international trade	**26,204**	**25.6**	26,912	26.3
Real estate, construction	**15,821**	**15.5**	14,699	14.4
Non-bank financial institutions	**5,509**	**5.4**	7,538	7.4
Other	**20,537**	**20.0**	21,075	20.6
Total commercial	**68,071**	**66.5**	70,224	68.7
Total	**102,418**	**100.0**	102,185	100.0

Bad debt provisions

Total provisions against loans and advances to customers amounted to £3,194 million at 31 December 1994 and represented 3.1 per cent of lending, compared with 3.8 per cent at the end of 1993. Midland reported a reduction of £544 million, arising mainly from the application of provisions following the debt restructuring agreement with Brazil and the sale of non-collateralised LDC debt.

The general improvement in credit quality of the Group's customer loan portfolio is reflected in the fall in non-performing loans and advances of £2,301 million, or 32 per cent, to £4,993 million. Non-performing loans amounted to 4.9 per cent of total loans and advances to customers, compared with 7.2 per cent at the end of December 1993. The majority of the reduction was in Midland, where there was a decline in both non-performing LDC debt and non-LDC debt.

Specific provisions against loans and advances to banks of £41,944 million (1993: £45,712 million) amounted to £72 million (1993: £248 million). Non-performing loans to banks dropped by £279 million to £91 million in 1994.

Customer loans and advances (£m)	**1994**	1993
Gross loans and advances	**102,418**	102,185
Suspended interest	**(429)**	(563)
	101,989	101,622
Provisions	**(3,194)**	(3,869)
Net loans and advances	**98,795**	97,753

Provisions to customer loans and advances (%)	**1994**	1993
Specific provisions	**2.4**	3.0
General provisions	**0.7**	0.8
Total provisions	**3.1**	3.8

Non-performing customer loans and provisions (£m)	**1994**	1993
Non-performing loans	**4,993**	7,294
Provisions	**3,194**	3,869

LDC exposure and provisions (£m)	**1994**	1993
LDC provisionable exposure	**1,443**	2,230
Provisions	**344**	903
Provisions as a percentage of LDC provisionable exposure (%)	**24**	40

Market Risk Management

Market risk

Market risk is the risk that interest rates, foreign exchange rates or equity and commodity prices will move relative to positions taken, causing profits or losses to the Group. Market risk arises on bank financial instruments which are either valued at current market prices (mark-to-market basis) or at cost plus any accrued interest (accruals basis).

The Group makes markets in interest rate and exchange rate derivative instruments as well as in debt, equity and other securities. Trading risks arise either from customer business or from position taking.

Market risk is managed within risk limits approved by the Group Executive Committee. Group Market Risk, an independent unit within Group Treasury, develops risk management policies and techniques, and reviews limit utilisation. Risk limits are determined for each portfolio, subject to restrictions on product, currency, interest rate repricing and market volatility risks. Liquidity considerations are also taken into account in determining the limits set. Only certain offices within major subsidiaries, with sufficient derivative product expertise and appropriate control systems, are authorised to trade derivative products. Actual risk levels compared with approved limits are monitored daily by each subsidiary and Group Market Risk.

Values at risk are computed for principal treasury centres across the Group on a regular basis and the potential loss due to a specified movement in market rates and prices estimated.

Foreign currency exposure

The Group's foreign currency exposures comprise: those which arise from foreign exchange dealing within Group Treasury; structural foreign currency translation exposures; and currency exposures originated by commercial banking businesses in the Group. The latter are transferred to local treasury units where they are managed together with exposures which result from dealing within limits approved by the Group Executive Committee.

The Group's structural foreign currency exposure is represented by the net asset value of the holding company's foreign currency equity and subordinated debt investments in its subsidiaries, branches and associated companies. These foreign currency investments amounted to the foreign currency equivalent of £7,100 million, or 66 per cent of shareholders' funds, at 31 December 1994, an increase from £6,792 million, or 73 per cent of shareholders' funds, at 31 December 1993. Gains or losses on structural foreign currency exposures are taken to reserves.

The higher level of structural foreign currency exposure, despite the general appreciation of sterling against most currencies which reduced the exposure, is due to the profit retentions in overseas subsidiaries, branches and associated companies. The lower proportion of shareholders' funds represented by the structural foreign currency exposure results from the appreciation of sterling and the increased capital held in the holding company as a result of dividend payments by subsidiaries.

Structural foreign exchange exposures are managed within the Group with the primary objective of ensuring, where practical, that the Group's and individual banking subsidiaries' tier 1 capital ratios are protected from the effect of changes in exchange rates. This is achieved by capital being denominated broadly in proportion to the corresponding foreign-currency denominated risk-weighted assets. Where appropriate, net foreign currency investments in overseas subsidiaries are hedged to meet this objective or to protect the sterling value of capital where the investment currency is judged to be fundamentally overvalued.

Interest rate exposure

The Group's interest rate exposures comprise those originating in its trading activities and structural interest rate exposures; both are managed under limits described above.

Structural interest rate risk arises primarily from the employment of non-interest bearing liabilities, such as some current accounts and shareholders' funds, as well as fixed rate loans and liabilities other than those generated by treasury business. Each major Group subsidiary has assessed the structural interest rate risks which arise in its business and has either transferred such risks to its local treasury unit or to separate books managed by the local asset and liability management committee. These interest rate positions are regularly monitored by subsidiaries' asset and liability management committees and, where necessary, quantitative models are used to assess the risks in these interest rate positions. While the primary objective of such interest rate risk management is to limit potential adverse effects of interest rate movements on net interest income, the subsidiaries also seek to enhance net interest income, subject to risk limits approved by the Group Executive Committee.

Liquidity Management

The Group manages the liquidity structure of its assets, liabilities and commitments so as to ensure that cash flows are sufficiently balanced within each of the subsidiaries. Where cash flow imbalances arise, the Group's policy is to establish minimum ratios of liquid assets to customer deposits.

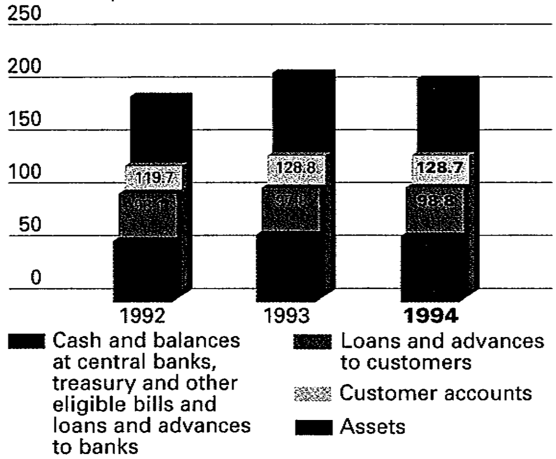
Core retail deposits (current accounts and savings deposits payable on demand or at short notice) form a significant part of the Group's overall funding. Considerable importance is attached to the stability of this core deposit base, achieved through the Group's diverse geographical retail banking activities. The Group prefers to grow its balance sheet through increasing core retail deposits where possible. Professional market funds are accessed for the purposes of providing additional funding, maintaining a presence in local money markets and optimising asset and liability maturities.

As at 31 December 1994 customer accounts totalled £128.7 billion, a decrease of 0.1 per cent from 31 December 1993. Deposits by banks fell by 32 per cent to £19.1 billion at 31 December 1994.

Customer current, deposit and savings accounts accounted for 87.1 per cent of the Group's deposit base at 31 December 1994 compared with 82.0 per cent at 31 December 1993. As at 31 December 1994, 76.8 per cent of the Group's customer accounts were deployed in loans and advances to customers compared with 75.9 per cent at 31 December 1993.

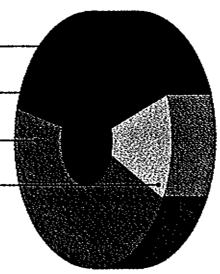
Cash and balances at central banks, treasury bills and other eligible bills and loans and advances to banks accounted for 26.3 per cent of total assets and 35.9 per cent of deposits at 31 December 1994 compared with 26.2 per cent and 34.6 per cent, respectively, at 31 December 1993.

Assets, deposits and advances (£b)



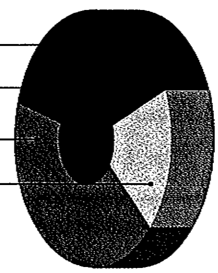
*Customer accounts and deposits by banks **1994***

	%	£b
Current	19.6	**29.0**
Savings	20.9	**30.9**
Other deposits	46.6	**68.8**
Deposits by banks	12.9	**19.1**
Total	100.0	**147.8**



Customer accounts and deposits by banks 1993

	%	£b
Current	19.0	29.8
Savings	20.4	32.0
Other deposits	42.6	67.1
Deposits by banks	18.0	28.2
Total	100.0	157.1



Off-Balance-Sheet Financial Instruments

Derivatives

Off-balance-sheet financial instruments, commonly referred to as derivatives, are contracts whose characteristics are derived from those of underlying assets, interest and exchange rates or indices.

Users of derivatives typically want to convert an unwanted risk generated by their business to a more acceptable risk, or cash. Derivatives provide an effective tool for companies to manage the financial risks associated with their business and, as a consequence, there has been a significant growth in derivatives transactions in recent years. They include futures, forwards, swap and options transactions in the foreign exchange, interest rate and equity markets. Deals are negotiated directly with customers, with the bank acting as a counterparty, or can be dealt through exchanges.

The Group, through the dealing operations of its subsidiaries, acts as an intermediary between a broad range of users, structuring deals to produce risk management products to suit individual customer needs. As a result, the Group can accumulate significant open positions in derivatives portfolios. These positions are managed constantly to ensure that they are within acceptable risk levels, with offsetting deals being undertaken to achieve this where necessary. As well as acting as a dealer, the Group also uses derivatives (principally interest rate swaps) in the management of its own asset and liability portfolios and structural positions.

The following table gives the outstanding notional principal amounts and the cost of replacing the contracts at current market rates if counterparties were not to meet their commitments under the contracts, as at 31 December 1993 and 31 December 1994, analysed by product type. The notional amounts of the instruments shown indicate the volume of transactions outstanding; they do not represent values at risk.

	1994		1993	
£m	Contract amount	Replacement cost	Contract amount	Replacement cost
Spot and forward foreign exchange	**261,015**	**2,754**	245,466	2,551
Other exchange rate contracts	**41,287**	**760**	33,778	487
Total exchange rate contracts	**302,302**	**3,514**	279,244	3,038
Interest rate swaps	**314,930**	**4,000**	221,302	4,834
Other interest rate contracts	**431,041**	**697**	333,507	730
Total interest rate contracts	**745,971**	**4,697**	554,809	5,564
Total	**1,048,273**	**8,211**	834,053	8,602

Other exchange rate contracts include currency options, currency futures and currency swaps. Other interest rate contracts include forward rate agreements, interest rate futures and interest rate option contracts, written and purchased.

At 31 December 1994, the total notional principal of outstanding contracts was £1,048 billion, compared with a value of £834 billion at 31 December 1993. The increase of £214 billion, or 26 per cent, was principally in interest rate contracts and is mainly due to an improvement in the marketing of swaps and increased market-making in forward rate agreements in a number of major treasury centres.

Interest rate swaps represent the most significant product through which interest rate risks are managed. The notional amount of interest rate swaps grew significantly during 1994, reflecting the demand for risk management products as a result of the increase in interest rate volatility experienced during the year.

Risks associated with derivatives

Derivative instruments are subject to both market risk and credit risk.

The market risk associated with derivatives can be significant since large positions can be accumulated with a substantially smaller initial outlay than required in cash markets. Recognising this, only certain offices within major subsidiaries with sufficient derivative product expertise and appropriate control systems are authorised to trade derivative products. The management of market risk arising from derivatives business is monitored by Group Market Risk.

Unlike assets recorded on the balance sheet, where the credit risk is typically the full amount of the principal value together with any unrealised interest accrued or mark-to-market gain, the credit risk relative to a derivative is principally the replacement cost of any contract with a positive mark-to-market gain and an estimate for the future fluctuation risk, using a future risk factor. The credit risk is therefore small in relation to a comparable balance sheet risk. In addition, to reduce further the potential for credit loss, the Group deals only with the most creditworthy counterparties, using netting arrangements where possible. Netting agreements allow for the net settlement of amounts payable or receivable from the same counterparty in the event of default.

The Group has examined and supports the recommendations of the Global Derivatives Study Group of the Group of 30 in respect of the management of risk in its derivatives businesses. It conforms with the principal recommendations made and is actively working on achieving full compliance.

The table analyses the replacement cost of all exchange rate and interest rate contracts with positive mark-to-market gains, after netting where permissible, by maturity and by category of counterparty.

The table shows that the replacement cost of financial instruments declined from £8.6 billion at 31 December 1993 to £8.2 billion at 31 December 1994, and that the risk is predominantly with banks and under 5 years.

	1994				1993
£m	Less than 1 year	1-5 years	Over 5 years	Total	Total
Governments	**57**	**27**	**3**	**87**	81
Banks	**3,846**	**2,572**	**414**	**6,832**	7,148
Non-bank financial institutions	**218**	**48**	**0**	**266**	244
Other sectors	**465**	**389**	**172**	**1,026**	1,129
Total **1994**	**4,586**	**3,036**	**589**	**8,211**	
Total 1993	3,861	3,918	823		8,602

Accounting for derivatives

Derivatives carried in dealing portfolios are marked-to-market on a daily basis, and gains and losses included in dealing profits. Derivatives used in balance sheet management to hedge open positions or specific assets or liabilities, are accounted for on an accruals basis, consistent with the underlying cash assets and liabilities held in these portfolios. In addition, interest rate swaps used for the strategic management of interest rate positions are accounted for on an accruals basis. Accounting policies related to derivatives are set out in more detail in Note 2j on the Accounts.

Financial Reporting

The 1994 financial accounts have been presented in the same format as last year, which reflected the application of the Companies Act 1985 (Bank Accounts) Regulations 1991 applicable to UK banking groups.

The accounting policies used in the preparation of the accounts are consistent with previous years, except as set out in Note 2 on the Accounts. For the 1994 accounts, Financial Reporting Standard 5 (FRS 5) 'Reporting the Substance of Transactions' has been implemented and the 1993 comparative data restated accordingly, resulting in total assets at 31 December 1993 increasing by £1.4 billion to £207.4 billion. The main impact on the Group's accounts has been that the criteria for netting loans and advances with related credit balances have been made more stringent, resulting in increased grossing up of balances. This is partially offset to the extent that netting is now mandatory where these criteria are met.

Where the sale or transfer of certain loans and advances under securitisation arrangements or sale and option to resell transactions are no longer effective under FRS 5, these have been restored to the balance sheet and a corresponding liability recorded.

The 1994 accounts also reflect a change in accounting policy for the translation of the results of overseas branches and subsidiary and associated undertakings into sterling. These results were previously translated at the rates of exchange ruling at the year-end, whereas they are now translated at the average rate, which more fairly reflects their contribution to the Group's results. As there is no material difference in the applicable exchange rates for 1993, the results for that year have not been restated. The effect of the change in accounting policy on the 1994 results was to increase profit attributable to shareholders by £29 million.

Consolidated Profit and Loss Account for the Year Ended 31 December 1994

1993 £m		Note	1994 £m	1994 HK$m	1994 US$m
	Interest receivable				
	— interest receivable and similar				
1,361	income arising from debt securities		**1,219**	*14,449*	*1,870*
	— other interest receivable and				
9,318	similar income		**9,556**	*113,267*	*14,659*
(6,241)	Interest payable		**(6,178)**	*(73,228)*	*(9,477)*
4,438	**Net interest income**		**4,597**	*54,488*	*7,052*
72	Dividend income	*3*	**70**	*830*	*107*
2,320	Fees and commissions receivable		**2,504**	*29,680*	*3,841*
(320)	Fees and commissions payable		**(173)**	*(2,051)*	*(265)*
1,089	Dealing profits		**261**	*3,094*	*400*
415	Other operating income		**365**	*4,326*	*560*
8,014	**Operating income**		**7,624**	*90,367*	*11,695*
(4,106)	Administrative expenses	*4*	**(4,222)**	*(50,043)*	*(6,477)*
(320)	Depreciation and amortisation	*21*	**(342)**	*(4,054)*	*(524)*
3,588	**Operating profit before provisions**		**3,060**	*36,270*	*4,694*
	Provisions				
(1,158)	— provisions for bad and doubtful debts	*14*	**(275)**	*(3,260)*	*(422)*
	— provisions for contingent liabilities				
(196)	and commitments	*28*	**(65)**	*(770)*	*(100)*
	Amounts written off fixed				
(32)	asset investments		**(6)**	*(71)*	*(9)*
2,202	**Operating profit**		**2,714**	*32,169*	*4,163*
	Profit on disposal of fixed assets				
287	and investments		**366**	*4,338*	*562*
95	Income from associated undertakings		**86**	*1,020*	*132*
2,584	**Profit on ordinary activities before tax**	*5*	**3,166**	*37,527*	*4,857*
(515)	Tax on profit on ordinary activities	*6*	**(829)**	*(9,827)*	*(1,272)*
2,069	**Profit on ordinary activities after tax**		**2,337**	*27,700*	*3,585*
	Minority interests				
(256)	— equity interests		**(267)**	*(3,164)*	*(410)*
(7)	— non-equity interests		**(17)**	*(202)*	*(26)*
	Profit for the financial year				
1,806	**attributable to shareholders**		**2,053**	*24,334*	*3,149*
(594)	Dividends	*8*	**(703)**	*(8,332)*	*(1,078)*
1,212	**Retained profit for the year**		**1,350**	*16,002*	*2,071*
Pence			Pence	*HK$*	*US$*
71.13	**Earnings per ordinary share**	*9*	**79.60**	*9.43*	*1.22*
68.77	**Headline earnings per ordinary share**	*9*	**76.84**	*9.11*	*1.18*
23.50	**Dividends per ordinary share**	*8*	**27.00**	*3.20*	*0.42*

Movements in reserves are set out in Note 32

Consolidated Balance Sheet at 31 December 1994

1993 £m		Note	1994 £m	*1994 HK$m*	*1994 US$m*
	ASSETS				
1,622	Cash and balances at central banks		**1,829**	*22,103*	*2,857*
2,483	Items in the course of collection from other banks		**2,196**	*26,538*	*3,430*
7,088	Treasury bills and other eligible bills	*10*	**9,298**	*112,366*	*14,523*
5,154	Hong Kong Government certificates of indebtedness	*11*	**5,006**	*60,504*	*7,819*
45,712	Loans and advances to banks	*12*	**41,944**	*506,893*	*65,517*
97,753	Loans and advances to customers	*13*	**98,795**	*1,193,938*	*154,318*
26,130	Debt securities	*17*	**21,345**	*257,954*	*33,341*
1,950	Equity shares	*18*	**1,979**	*23,916*	*3,091*
556	Interests in associated undertakings	*19*	**420**	*5,075*	*656*
134	Other participating interests	*20*	**92**	*1,111*	*144*
4,781	Tangible fixed assets	*21*	**4,917**	*59,421*	*7,680*
11,799	Other assets	*23*	**11,722**	*141,659*	*18,310*
2,285	Prepayments and accrued income		**1,975**	*23,867*	*3,085*
207,447	Total assets		**201,518**	*2,435,345*	*314,771*
	LIABILITIES				
5,159	Hong Kong currency notes in circulation	*11*	**5,011**	*60,564*	*7,827*
28,245	Deposits by banks	*24*	**19,127**	*231,149*	*29,876*
128,843	Customer accounts	*25*	**128,707**	*1,555,424*	*201,040*
1,399	Items in the course of transmission to other banks		**982**	*11,867*	*1,534*
6,444	Debt securities in issue	*26*	**8,782**	*106,130*	*13,717*
18,417	Other liabilities	*27*	**18,511**	*223,706*	*28,914*
2,251	Accruals and deferred income		**2,055**	*24,834*	*3,210*
	Provisions for liabilities and charges	*28*			
253	— deferred taxation		**323**	*3,903*	*505*
349	— other provisions for liabilities and charges		**348**	*4,205*	*544*
	Subordinated liabilities	*29*			
1,859	— undated loan capital		**1,761**	*21,281*	*2,751*
3,328	— dated loan capital		**3,448**	*41,668*	*5,386*
	Minority interests				
1,336	— equity		**1,454**	*17,571*	*2,271*
230	— non-equity	*30*	**219**	*2,646*	*342*
2,111	Called up share capital	*31*	**2,090**	*25,258*	*3,265*
378	Share premium account	*32*	**319**	*3,855*	*498*
148	Reserves	*32*	**148**	*1,789*	*231*
1,421	Revaluation reserve	*32*	**1,478**	*17,862*	*2,309*
5,276	Profit and loss account	*32*	**6,755**	*81,633*	*10,551*
9,334	Shareholders' funds		**10,790**	*130,397*	*16,854*
207,447	Total liabilities		**201,518**	*2,435,345*	*314,771*
	MEMORANDUM ITEMS				
	Contingent liabilities	*34*			
1,398	— acceptances and endorsements		**1,325**	*16,013*	*2,070*
10,733	— guarantees and assets pledged as collateral security		**11,893**	*143,727*	*18,577*
352	— other contingent liabilities		**183**	*2,212*	*286*
12,483			**13,401**	*161,952*	*20,933*
57,807	Commitments	*34*	**60,897**	*735,940*	*95,121*

W Purves, *Group Chairman*

Company Balance Sheet at 31 December 1994

1993 £m		Note	1994 £m	*1994 HK$m*	*1994 US$m*
	FIXED ASSETS				
11	Tangible assets	*21*	**11**	*133*	*17*
	Investments	*22*			
9,559	— shares in Group undertakings		**10,348**	*125,056*	*16,164*
1,077	— loans to Group undertakings		**862**	*10,417*	*1,346*
149	— other investments other than loans		**147**	*1,776*	*230*
10,796			**11,368**	*137,382*	*17,757*
	CURRENT ASSETS				
	Debtors				
365	— amounts owed by Group undertakings		**1,173**	*14,176*	*1,832*
126	— amounts owed by Group undertakings (falling due after more than 1 year)		**312**	*3,770*	*488*
3	— other debtors		**4**	*48*	*6*
	Cash at bank and in hand				
210	— balances with Group undertakings		**384**	*4,641*	*600*
704			**1,873**	*22,635*	*2,926*
	CREDITORS: amounts falling due within one year				
(57)	Amounts owed to Group undertakings		**(217)**	*(2,622)*	*(339)*
(83)	Other creditors		**(95)**	*(1,148)*	*(149)*
(119)	Taxation		**(165)**	*(1,994)*	*(258)*
(418)	Proposed dividend	*8*	**(495)**	*(5,982)*	*(773)*
(677)			**(972)**	*(11,746)*	*(1,519)*
27	**NET CURRENT ASSETS**		**901**	*10,889*	*1,407*
10,823	**TOTAL ASSETS LESS CURRENT LIABILITIES**		**12,269**	*148,271*	*19,164*
	CREDITORS: amounts falling due after more than one year				
	Subordinated liabilities	*29*			
(827)	— owed to third parties		**(819)**	*(9,898)*	*(1,279)*
(235)	— owed to Group undertakings		**(223)**	*(2,695)*	*(348)*
(401)	Amounts owed to Group undertakings		**(296)**	*(3,577)*	*(463)*
	PROVISIONS FOR LIABILITIES AND CHARGES				
(26)	Deferred taxation	*28*	**(141)**	*(1,704)*	*(220)*
9,334	**NET ASSETS**		**10,790**	*130,397*	*16,854*
	CAPITAL AND RESERVES				
2,111	Called up share capital	*31*	**2,090**	*25,258*	*3,265*
378	Share premium account	*32*	**319**	*3,855*	*498*
4,003	Revaluation reserve	*32*	**5,451**	*65,875*	*8,514*
2,842	Profit and loss account	*32*	**2,930**	*35,409*	*4,577*
9,334			**10,790**	*130,397*	*16,854*

W Purves, *Group Chairman*

Statement of Total Consolidated Recognised Gains and Losses for the Year Ended 31 December 1994

	1994 **£m**	1993 £m
Profit for the financial year attributable to shareholders	**2,053**	*1,806*
Unrealised surplus on revaluation of investment properties	**125**	—
Permanent diminution in value of land and buildings	**(32)**	*(123)*
Exchange and other movements	**(363)**	*149*
Total recognised gains and losses for the year	**1,783**	*1,832*

Reconciliation of Movements in Consolidated Shareholders' Funds for the Year Ended 31 December 1994

	1994 **£m**	1993 £m
Profit for the financial year attributable to shareholders	**2,053**	*1,806*
Dividends	**(703)**	*(594)*
	1,350	*1,212*
Other recognised gains and losses relating to the year	**(270)**	*26*
New share capital subscribed	**8**	*6*
Arising on shares issued in lieu of dividend	**368**	*115*
Goodwill on acquisition of subsidiary undertakings	**—**	*(36)*
Net addition to shareholders' funds	**1,456**	*1,323*
Shareholders' funds at 1 January	**9,334**	*8,011*
Shareholders' funds at 31 December	**10,790**	*9,334*

No note of historical cost profits and losses has been presented as there is no material difference between the Group's results as disclosed in the consolidated profit and loss account and the results on an unmodified historical cost basis.

Consolidated Cash Flow Statement for the Year Ended 31 December 1994

	Note	1994 £m	1993 £m
Net cash (outflow)/inflow from operating activities	35	(1,249)	11,010
Returns on investments and servicing of finance:			
Income received on investment securities		706	630
Dividends received from associated undertakings		43	12
Interest paid on finance leases and similar hire purchase contracts		(11)	(9)
Interest paid on loan capital		(288)	(231)
Dividend paid to minority interests			
— equity		(115)	(109)
— non-equity		(17)	(7)
Ordinary dividends paid		(254)	(417)
Net cash inflow/(outflow) from returns on investments and servicing of finance		64	(131)
Taxation paid		(601)	(332)
Investing activities:			
Purchase of investment securities		(10,555)	(11,003)
Proceeds from sale of investment securities		11,709	6,074
Purchase of tangible fixed assets		(618)	(368)
Proceeds of sale of tangible fixed assets		174	285
Net cash outflow from acquisition of subsidiary undertakings		—	(183)
Net cash inflow from disposal of subsidiary undertakings		20	—
Purchase of interest in associated undertakings and other participating interests		(17)	(112)
Proceeds from partial disposal of associated undertaking		147	—
Net cash inflow/(outflow) from investing activities		860	(5,307)
Net cash (outflow)/inflow before financing		(926)	5,240
Financing:			
Issue of ordinary share capital		8	6
Issue of preference share capital		—	164
Loan stock issued		420	1,134
Loan capital repaid		(301)	(133)
Net cash inflow from financing	36	127	1,171
(Decrease)/Increase in cash and cash equivalents	37	(799)	6,411

Notes on the Accounts

1 Basis of preparation

a The accounts have been prepared under the historical cost convention, as modified by the revaluation of certain investments and land and buildings, and in accordance with applicable accounting standards.

The consolidated accounts are prepared in accordance with the special provisions of Part VII Chapter II of the Companies Act 1985 ('the Act') relating to banking groups. The consolidated accounts comply with Schedule 9 and the accounts of HSBC Holdings plc ('the Company') comply with Schedule 4 to the Act.

As permitted by Section 230 of the Act, no profit and loss account is presented for the Company.

The accounting policies used in the preparation of these accounts are consistent with previous years except for the changes set out in Note 2b below, which reflect the new requirements of Financial Reporting Standard ('FRS') 5, 'Reporting the Substance of Transactions', and in Note 2i below, which relate to the change in accounting policy for the translation of the results of overseas branches and subsidiary and associated undertakings to average rates of exchange.

b The consolidated accounts comprise the accounts of the Company and its subsidiary and associated undertakings (together 'the Group'). Accounts of subsidiary undertakings are made up to 31 December, except in the case of Midland Life Limited, whose accounts are made up to 31 August and for which, therefore, the Group uses interim accounts, made up to 31 December 1994, and Hongkong Bank of Canada, whose accounts are made up to 31 October annually. The consolidated accounts include the attributable share of the results and reserves of associated undertakings, based on accounts made up to dates not earlier than six months prior to 31 December.

All significant intra-Group transactions have been eliminated on consolidation.

2 Principal accounting policies

a *Income recognition*

Interest income is recognised in the profit and loss account as it accrues, except in the case of doubtful debts (Note 2b).

Fee income is accounted for in the period when receivable, except where the fee is charged to cover the costs of a continuing service to, or risk borne for, the customer, or is interest in nature. In these cases, the fee is recognised on an appropriate basis over the relevant period.

b *Loans and advances and doubtful debts*

FRS 5 has been implemented during the year and comparative data have been restated accordingly (see Note 33e). The criteria for netting loans and advances with related credit balances have been changed, resulting in increased grossing up of balances. However, this is offset to the extent that netting is now mandatory rather than permissible where these criteria are met. Where transfers of certain loans and advances under securitisation arrangements or sale and option to resell transactions are no longer effective under FRS 5, these loans and advances have been restored to the balance sheet, and a corresponding liability recorded.

Specific provision is made for doubtful debts as and when they are so considered and, in addition, amounts have been set aside as general provisions for doubtful debts. The specific element relates to individual banking relationships; the general element relates to other exposures not separately identified but known from experience to exist in any portfolio of banking relationships. When there is no longer any realistic prospect of recovery, the outstanding debt is written off.

Interest on doubtful debts is credited to a suspense account which is netted in the balance sheet against the relevant balances.

Assets acquired in exchange for advances in order to achieve an orderly realisation continue to be reported as advances. The asset acquired is recorded at the carrying value of the advance disposed of at the date of the exchange, and provisions are based on any subsequent deterioration in its value.

c *Debt securities and equity shares*

Debt securities and equity shares intended to be held on a continuing basis are disclosed as investment securities and are included in the balance sheet at cost less provision for any permanent diminution in value.

2 Principal accounting policies *(continued)*

Where dated investment securities have been purchased at a premium or discount, these premiums and discounts are amortised through the profit and loss account over the period from the date of purchase to the date of maturity. If the maturity is at the borrowers' option within a specified range of years, the maturity date which gives the more conservative result is adopted. These securities are included in the balance sheet at cost adjusted for the amortisation of premiums and discounts arising on acquisition. The amortisation of premiums and discounts is included in 'Interest receivable'. Any profit or loss on realisation of these securities is recognised in the profit and loss account as it arises and included in 'Profit on disposal of fixed assets and investments'.

Debt securities held for the purpose of hedging are valued on the same basis as the liabilities which are being hedged.

Other debt securities and equity shares are included in the balance sheet at market value. Changes in the market value of such assets are recognised in the profit and loss account as 'Dealing profits' as they arise.

Where securities are sold subject to a commitment to repurchase them at a predetermined price, they remain on the balance sheet and a liability is recorded in respect of the consideration received. Conversely, securities purchased under analogous commitments to resell are not recognised on the balance sheet and the consideration paid is recorded in 'Loans and advances to customers' or 'Loans and advances to banks'.

d *Subsidiary and associated undertakings and other participating interests*

i The Company's investments in subsidiary undertakings are stated at attributable net asset values. Changes in net tangible assets of subsidiary undertakings are accounted for as movements in the revaluation reserve.

ii Interests in associated undertakings are stated at the Group's attributable share of the net tangible assets of the relevant companies.

iii Other participating interests are investments in the shares of undertakings which are held on a long-term basis for the purpose of securing a contribution to the Group's business, other than subsidiary or associated undertakings. Other participating interests are stated at cost less any permanent diminution in value.

iv Goodwill arising on the acquisition of subsidiary or associated undertakings, being the excess of the cost of acquisition over the fair value of the Group's share of separable net assets acquired, is charged against reserves in the year of acquisition. At the date of disposal of subsidiary or associated undertakings, goodwill is reinstated in reserves and included in the calculation of the profit on disposal of the undertaking.

e *Tangible fixed assets*

i Land and buildings are stated at valuation or cost less depreciation calculated to write off the assets over their estimated useful lives as follows:

— freehold land and land held on leases with more than 50 years to expiry are not depreciated.

— land held on leases with 50 years or less to expiry is depreciated over the unexpired terms of the leases.

— buildings and improvements thereto are depreciated on cost at the greater of 2% per annum on the straight line basis or over the unexpired terms of the leases.

ii Equipment, fixtures and fittings are stated at cost less depreciation calculated on the straight line basis to write off the assets over their estimated useful lives, which are generally between 5 years and 20 years.

iii The Group holds certain properties as investments. No depreciation is provided in respect of such properties other than leaseholds with 20 years or less to expiry. Investment properties are included in the balance sheet at their open market value and the aggregate surplus or deficit, where material, is transferred to the investment property revaluation reserve.

f *Finance and operating leases*

i Assets leased to customers under agreements which transfer substantially all the risks and rewards associated with ownership, other than legal title, are classified as finance leases. Where the Group is a lessor under finance leases the amounts due under the leases, after deduction of unearned charges, are included in 'Loans and advances to customers' or 'Loans and advances to banks'. Finance charges receivable are recognised over the periods of the leases in proportion to the funds invested.

2 Principal accounting policies *(continued)*

ii Where the Group is a lessee under finance leases, the leased assets are capitalised and included in 'Equipment, fixtures and fittings' and the corresponding liability to the lessor is included in 'Other liabilities'. Finance charges payable are recognised over the periods of the leases based on the interest rates implicit in the leases.

iii All other leases are classified as operating leases and, where the Group is the lessor, are included in tangible fixed assets. Rentals payable and receivable under operating leases are accounted for on the straight line basis over the periods of the leases and are included in 'Administrative expenses' and 'Other operating income' respectively.

g *Deferred taxation*

Deferred taxation is provided on timing differences, using the liability method, between the accounting and taxation treatment of income and expenditure. Provision is made for deferred tax only to the extent that it is probable that an actual liability will crystallise.

h *Pension and other post-retirement benefits*

The Group operates a number of pension and other post-retirement benefit schemes throughout the world and the major schemes are of the defined benefit type.

For UK pension schemes annual contributions are made, on the advice of qualified actuaries, for funding of retirement benefits in order to build up reserves for each scheme member during the employee's working life and used to pay to the employee or dependant a pension after retirement. The costs of providing these benefits are charged to the profit and loss account on a regular basis.

Arrangements for staff retirement benefits in overseas locations vary from country to country and are made in accordance with local regulations and custom. The pension cost of the major overseas schemes is assessed in accordance with the advice of qualified actuaries so as to recognise the cost of pensions on a systematic basis over employees' service lives.

The cost of providing post-retirement health care benefits, which is assessed in accordance with the advice of qualified actuaries, is recognised on a systematic basis over employees' service lives. At 1 January 1993, there was an accumulated obligation in respect of these benefits relating to current and retired employees. This is being charged in the profit and loss account in equal instalments over 20 years.

i *Foreign currencies*

i Assets and liabilities denominated in foreign currencies are translated into sterling at the rates of exchange ruling at the year-end. The results of overseas branches and subsidiary and associated undertakings are translated into sterling at the average rates of exchange for the year. Previously, these results were translated at the rates of exchange ruling at the year-end (the closing rate method). The Directors believe that, as the results of overseas branches and subsidiary and associated undertakings arise throughout the accounting period, translating them at average rates of exchange more fairly reflects their contribution to the Group's results. This change results in profit on ordinary activities after tax in 1994 being higher by £29 million than would have been the case under the closing rate method. As there is no material difference in applicable exchange rates for 1993, the 1993 results have not been restated.

ii Exchange differences arising from the retranslation of opening foreign currency net investments and the related cost of hedging and exchange differences arising from retranslation of the result for the year from the average rate to the exchange rate ruling at the year-end are accounted for in reserves.

iii Other exchange differences are recognised in the profit and loss account.

j *Off-balance-sheet financial instruments*

Off-balance-sheet financial instruments arise from futures, forward, swap and option transactions undertaken by the Group in the foreign exchange, interest rate and equity markets.

Accounting for these instruments is dependent upon whether the transactions are undertaken for dealing purposes, to hedge risk, or as part of the management of asset and liability portfolios.

2 Principal accounting policies *(continued)*

Transactions undertaken for dealing purposes are marked to market value and the net present value of the gain or loss arising is recognised in the profit and loss account as 'Dealing profits', after appropriate deferrals for unearned credit margin and future servicing costs.

Transactions designated as hedges are accounted for on an equivalent basis to the assets, liabilities or net positions they are hedging. Any profit or loss is recognised on the same basis as that arising from the related assets, liabilities or positions.

Interest rate swap transactions undertaken as part of the management of asset and liability portfolios are separately identified and income or expense is accrued and included in 'Interest receivable' or 'Interest payable'.

Assets, including gains, resulting from off-balance-sheet interest rate and exchange rate contracts which are marked to market are included in 'Other assets'. Liabilities, including losses, resulting from such contracts, are included in 'Other liabilities'.

3 Dividend income

	1994	1993
	£m	£m
Income from equity shares	**67**	65
Income from participating interests other than associated undertakings	**3**	7
	70	72

4 Administrative expenses

a

	1994	1993
	£m	£m
Staff costs		
— wages and salaries	**2,304**	2,203
— social security costs	**129**	113
— other pension costs (Note 4b below)	**213**	186
	2,646	2,502
Premises and equipment (excluding depreciation)	**596**	598
Other administrative expenses	**980**	1,006
	4,222	4,106

Premises and equipment costs now include property taxes, repairs and maintenance, and expenditure on utilities as well as rental costs. Comparative data have been restated accordingly.

The average number of persons employed by the Group during the year was made up as follows:

	1994	1993
	Number	Number
Commercial banking	**102,741**	99,870
Investment banking	**4,120**	4,157
	106,861	104,027

b *Retirement benefits*

The Group operates some 95 pension schemes throughout the world, with a total pension cost of £213 million (1993: £186 million), of which £88 million (1993: £82 million) relates to overseas schemes. Of the overseas schemes, £15 million (1993: £16 million) has been determined in accordance with best practice and regulations in the United States and Canada.

The majority of the schemes, which cover 84% of the Group's employees, are funded defined benefit schemes with assets in the case of the larger schemes held in trust funds separate from the Group. The pension cost relating to these schemes was £200 million (1993: £175 million) which is assessed in accordance with the

4 Administrative expenses *(continued)*

advice of qualified actuaries; the schemes are reviewed at least on a triennial basis or in accordance with local practice and regulations. The actuarial assumptions used to calculate the projected benefit obligations of the Group's pension schemes vary according to the economic conditions of the country in which they are situated.

For the principal UK scheme, the Midland Bank Pension Scheme, the latest valuation was made at 31 December 1993 and was performed by P Lofthouse, Fellow of the Institute of Actuaries, of R Watson & Sons. At that date, the market value of the scheme's assets was £3,685 million. The actuarial value of the assets represented 99.5% of the benefits accrued to members, after allowing for expected future increases in earnings, and the resulting deficit amounted to £18 million. On the basis of the actuaries' recommendations, contributions were increased from 14.0% to 16.1% of pensionable salaries with effect from 1 January 1994, to remain at that percentage at least until the next actuarial valuation. The actuarial method used is the projected unit method and the main assumptions used in this valuation were a long-term investment return of 9.2% per annum, salary increases of 6.3% per annum, equity dividend increases and rental growth of 4.5% per annum and post-retirement pension increases of 4.0% per annum.

For the principal non-UK scheme, the Hong Kong Local Staff Retirement Benefits Scheme, the latest valuation was made at 31 December 1993 and was performed by E Chiu and V Lo, Fellows of the Society of Actuaries, of HSBC Life (International) Limited. At that date, the market value of the scheme's assets was £266 million. The actuarial value of the assets represented 101% of the benefits accrued to members, after allowing for expected future increases in earnings, and the resulting surplus amounted to £3 million. The actuarial method used is the projected unit method and the main assumptions used in this valuation were a long-term investment return of 9% per annum and salary increases of 8% per annum.

The Midland Bank Pension Scheme and the Hong Kong Local Staff Retirement Benefits Scheme cover 53% of the Group's employees.

The pension cost for defined contribution schemes, which cover 12% of the Group's employees, was £13 million (1993: £11 million).

The Group also provides post-retirement health care benefits under schemes, mainly in the UK and also in the United States and Canada. The charge relating to these schemes, which are unfunded, is £25 million for the year (1993: £27 million). The latest actuarial review as at 31 December 1994 estimated the present value of the accumulated post-retirement benefit obligation at £192 million (1993: £198 million), of which £40 million (1993: £21 million) has been provided. The actuarial assumptions used to estimate this obligation vary according to the claims experience and economic conditions of the country in which the scheme is situated. For the UK schemes, the main financial assumptions used at 31 December 1994 are price inflation of 4.5% per annum, health care claims cost escalation of 8% per annum and a discount rate of 8.5% per annum. New entrants are no longer permitted to the UK scheme.

c *Directors' emoluments*

The aggregate emoluments of the Directors of the Company, computed in accordance with Part I of Schedule 6 of the Act were:

	1994	1993
	£000	£000
Fees	**397**	440
Salaries and other emoluments	**3,196**	3,671
Discretionary bonuses	**465**	255
Pension contributions	**294**	457
	4,352	4,823

4 Administrative expenses *(continued)*

The emoluments of the Directors, excluding pension contributions, are within the following bands:

£	**1994 Number of Directors**	1993 Number of Directors	£	**1994 Number of Directors**	1993 Number of Directors
10,001– 15,000	**2**	3	370,001–375,000	**1**	2
15,001– 20,000	**2**	—	395,001–400,000	**—**	1
25,001– 30,000	**2**	4	440,001–445,000	**—**	1
30,001– 35,000	**3**	3	495,001–500,000	**—**	1
55,001– 60,000	**1**	—	520,001–525,000	**1**	—
60,001– 65,000	**1**	2	560,001–565,000	**1**	—
65,001– 70,000	**1**	—	630,001–635,000	**1**	—
85,001– 90,000	**1**	—	720,001–725,000	**—**	1
215,001–220,000	**—**	1	810,001–815,000	**1**	—
290,001–295,000	**1**	—	965,001–970,000	**—**	1
355,001–360,000	**1**	—			

The emoluments of the Chairman and the highest paid Director were:

	1994 Chairman £000	**1994 Highest paid Director £000**	1993 Chairman £000
Fees	**15**	**13**	15
Salary and other emoluments	**518**	**802**	910
Discretionary bonuses	**100**	**—**	40
Pension contributions	**—**	**65**	96
	633	**880**	1,061

The highest paid Director in 1994 discharged his duties mainly outside the United Kingdom. The above information is provided on the basis that would have applied had he discharged those duties within the United Kingdom. In 1993, the Chairman was the highest paid Director and remains the highest paid Director of those Directors who discharge their duties mainly in the United Kingdom. The emoluments of the highest paid Director in 1994 and of the Chairman for part of 1993 include housing and other expatriate benefits in kind which are normal within the locations in which they were employed and which constitute a significant portion of their emoluments.

In addition, pensions in respect of past services of £30,000 (1993: £ nil) were paid.

Discretionary bonuses for Directors are based on a combination of individual and corporate performance and are determined by the Remuneration Committee. Details of Directors' share options and emoluments are disclosed in the 'Report of the Directors' (see pages 25 to 31).

Five Directors waived the right to receive emoluments totalling £69,965 (1993: five Directors £71,405).

d *Auditors' remuneration*

Auditors' remuneration amounted to £9.1 million (1993: £9.3 million). £4 million (1993: £2.8 million) was paid to the Company's auditors and their associates for non-audit work.

5 Profit on ordinary activities before tax

Profit on ordinary activities before tax is stated after:

	1994 £m	1993 £m
i *Income*		
Aggregate rentals receivable, including capital repayments, under		
— finance leases	1,887	1,981
— operating leases	127	82
Income from listed investments	1,072	1,202
Profits less losses on debt securities and equities dealing	(79)	359
Profits less losses on disposal of investment securities	295	219
ii *Charges*		
Exceptional item — provision in respect of British & Commonwealth Holdings plc litigation (see Note 38)	—	125
Charges incurred with respect to subordinated liabilities	298	305
Finance charges in respect of finance leases and similar hire purchase contracts	15	21
Hire of plant and machinery	64	87

Profit on the disposal of fixed assets and investments attracted a tax charge of £48 million (1993: £48 million). Of the after-tax amount, £59 million (1993: £53 million) is attributable to minority interests.

6 Tax on profit on ordinary activities

The charge for taxation comprises:

	1994 £m	1993 £m
United Kingdom corporation tax charge	350	128
Relief for overseas taxation	(22)	(36)
	328	92
Overseas taxation	498	392
Deferred taxation	(7)	15
	819	499
Associated undertakings	10	16
	829	515

The Company and its subsidiary undertakings in the UK provide for UK corporation tax at 33% (1993: 33%). Overseas tax includes Hong Kong profits tax of £200 million (1993: £207 million). Subsidiary undertakings in Hong Kong provide for Hong Kong profits tax at the rate of 16.5% (1993: 17.5%) on the profits for the year assessable in Hong Kong. Other overseas subsidiary undertakings and overseas branches provide for taxation in the countries in which they operate at the appropriate rates of taxation.

7 Profit of the Company

The profit of the Company for the year is £419 million (1993: £184 million).

8 Dividends

	1994		1993	
	Pence per share	£m	Pence per share	£m
Interim	8.00	208	7.00	176
Proposed final	19.00	495	16.50	418
	27.00	703	23.50	594

Of the interim dividend for 1994, £36 million (1993: £45 million) was settled by the issue of shares. Of the final dividend for 1993, £336 million (1992: £70 million) was settled by the issue of shares in 1994. The issue of shares in respect of the final dividend for 1993 related to the enhanced scrip dividend.

9 Earnings per ordinary share

Earnings per ordinary share is calculated by dividing the earnings of £2,053 million (1993: £1,806 million) by the weighted average number of ordinary shares in issue in 1994 of 2,579 million (1993: 2,539 million). The average number of shares in issue in both 1994 and 1993 has been adjusted to reflect the bonus element of the enhanced scrip dividend alternative taken up in lieu of the final dividend for 1993. Fully diluted earnings per share is not materially different from the basic earnings per ordinary share shown.

As the headline earnings per share measure has now gained widespread acceptance, this has been calculated in accordance with the definitions in the Institute of Investment Management and Research ('IIMR') Statement of Investment Practice No. 1, 'The Definition of IIMR Headline Earnings', as follows:

	1994	1993
	Pence	Pence
Earnings per ordinary share	**79.60**	71.13
Adjustments:		
Profits on sale of tangible fixed assets	**(0.12)**	(1.81)
Profit on sale of subsidiary undertaking (1993: adjusted for minority interest)	**(0.16)**	(0.55)
Profit on partial sale of associated undertaking	**(2.48)**	—
Headline earnings per ordinary share	**76.84**	68.77

10 Treasury bills and other eligible bills

	1994	1993
	£m	£m
Treasury bills and similar securities	**8,342**	5,818
Other eligible bills	**956**	1,270
	9,298	7,088

None of the treasury and other eligible bills has been accounted for as investment securities.

11 Hong Kong currency notes in circulation

	1994	1993
	£m	£m
Authorised note issue (HK$60 million)	**5**	5
Excess note issue (HK$60,504 million)	**5,006**	5,154
	5,011	5,159

The authorised note issue is secured by the deposit of investments having a market value of £6 million (1993: £6 million). The excess note issue is secured by the deposit of funds in respect of which the Hong Kong Government certificates of indebtedness are held.

Notes on the Accounts *(continued)*

12 Loans and advances to banks

	1994 £m	1993 £m
Remaining maturity:		
— repayable on demand	**3,390**	1,763
— 1 month or less but not on demand	**26,319**	30,125
	29,709	31,888
— 3 months or less but over 1 month	**6,959**	9,328
— 1 year or less but over 3 months	**3,796**	3,104
— 5 years or less but over 1 year	**414**	465
— over 5 years	**1,138**	1,175
Specific bad and doubtful debt provisions (Note 14)	**(72)**	(248)
	41,944	45,712

The bad and doubtful debt provisions against loans and advances to banks relate principally to less developed country exposures.

	1994 £m	1993 £m
Amounts include:		
Due from associated undertakings		
— unsubordinated	**68**	48
Due from other undertakings in which the Group has a participating interest		
— unsubordinated	**—**	2

13 Loans and advances to customers

	1994 £m	1993 £m
Remaining maturity:		
— repayable on demand or at short notice	**28,456**	31,678
— 3 months or less but not repayable on demand or at short notice	**8,303**	8,901
— 3 months or less	**36,759**	40,579
— 1 year or less but over 3 months	**12,397**	11,971
— 5 years or less but over 1 year	**28,477**	24,565
— over 5 years	**24,356**	24,507
General and specific bad and doubtful debt provisions (Note 14)	**(3,194)**	(3,869)
	98,795	97,753

	1994 £m	1993 £m
Amounts include:		
Subordinated	**83**	76
Securitised advances not qualifying for separate or linked presentation under FRS 5	**453**	667
Due from associated undertakings		
— unsubordinated	**190**	213
Due from other undertakings in which the Group has a participating interest		
— unsubordinated	**21**	62

14 Provisions for bad and doubtful debts

	Provisions against advances			Suspended
	Specific	*General*	*Total*	*interest*
	£m	**£m**	**£m**	**£m**
At 1 January 1994	**3,336**	**781**	**4,117**	**649**
Amounts written off	**(1,177)**	**—**	**(1,177)**	**(149)**
Recoveries of advances written off in previous years	**124**	**—**	**124**	**—**
Charge to profit and loss account	**259**	**16**	**275**	**—**
Interest suspended during the year	**—**	**—**	**—**	**136**
Suspended interest recovered	**—**	**—**	**—**	**(121)**
Exchange and other movements	**(36)**	**(37)**	**(73)**	**(21)**
At 31 December 1994	**2,506**	**760**	**3,266**	**494**

Included in:	
Loans and advances to banks (Note 12)	**72**
Loans and advances to customers (Note 13)	**3,194**
	3,266

	Provisions against advances			Suspended
	Specific	*General*	*Total*	*interest*
	£m	£m	£m	£m
At 1 January 1993	3,587	692	4,279	799
Amounts written off	(1,448)	—	(1,448)	(212)
Recoveries of advances written off in previous years	104	—	104	—
Charge to profit and loss account	1,045	113	1,158	—
Interest suspended during the year	—	—	—	221
Suspended interest recovered	—	—	—	(199)
Exchange and other movements	48	(24)	24	40
At 31 December 1993	3,336	781	4,117	649

Included in:	
Loans and advances to banks (Note 12)	248
Loans and advances to customers (Note 13)	3,869
	4,117

The total of advances, net of suspended interest, on which interest is being placed in suspense, is as follows:

	1994	1993
	£m	£m
Gross	**2,407**	3,994
Net of specific provisions	**998**	1,866

15 Less developed country exposure

	1994	1993
	£m	£m
Total less developed country exposures to banks and customers (net of provisions in respect of commercial risk)	**1,443**	2,230
Total accrued interest	**60**	203
	1,503	2,433
Less developed country risk provisions	**(344)**	(903)
Suspended interest	**(60)**	(192)
Net exposure to less developed countries	**1,099**	1,338
As a percentage of shareholders' funds	**10.2%**	14.3%

15 Less developed country exposure *(continued)*

Less developed country provisionable exposure includes the holding of par and discount bonds issued as a result of debt restructuring by Argentina, Brazil, Mexico, the Philippines and Venezuela. The principal amount of these bonds is secured by US Treasury instruments and as at 31 December 1994 the gross carrying value was £1,136 million (1993: £1,060 million).

16 Concentrations of exposure

The following industry concentrations, gross of specific provisions, are in excess of 10% of total gross advances to customers:

	1994	1993
	£m	£m
Consumer:		
Residential mortgages	**23,450**	21,418
Other advances to individuals	**10,897**	10,543
Commercial:		
Commercial, industrial and international trade	**26,204**	26,912
Commercial real estate	**15,821**	14,699

17 Debt securities

	1994		1993	
	Book value	*Market valuation*	*Book value*	*Market valuation*
	£m	**£m**	£m	£m
Issued by public bodies				
Investment securities				
— government securities	**6,783**	**6,634**	6,993	7,021
— other public sector securities	**429**	**412**	364	374
	7,212	**7,046**	7,357	7,395
Other securities				
— government securities	**3,785**		8,576	
— other public sector securities	**198**		178	
	11,195		16,111	
Issued by other bodies				
Investment securities				
— bank and building society certificates of deposit	**1,058**	**1,036**	866	870
— other debt securities	**3,025**	**3,004**	4,032	4,077
	4,083	**4,040**	4,898	4,947
Other securities				
— bank and building society certificates of deposit	**2,839**		2,016	
— other debt securities	**3,228**		3,105	
	10,150		10,019	
	21,345		26,130	
Due within 1 year	**8,108**		8,032	
Due 1 year and over	**13,237**		18,098	
	21,345		26,130	

17 Debt securities *(continued)*

	1994		1993	
	Book value	*Market valuation*	*Book value*	*Market valuation*
	£m	**£m**	£m	£m
Amounts include:				
Subordinated debt securities	**105**		22	
Due from other undertakings in which the Group has a participating interest —unsubordinated	**—**		10	
Unamortised premiums net of discounts on investment securities	**64**		165	
Investment securities				
— listed on a recognised UK exchange	**2,732**	**2,694**	2,618	2,621
— listed in Hong Kong	**684**	**673**	466	463
— listed elsewhere	**3,777**	**3,657**	5,476	5,531
— unlisted	**4,102**	**4,062**	3,695	3,727
	11,295	**11,086**	12,255	12,342
Other debt securities				
— listed on a recognised UK exchange	**1,125**		2,313	
— listed in Hong Kong	**127**		53	
— listed elsewhere	**4,456**		6,775	
— unlisted	**4,342**		4,734	
	21,345		26,130	

Where securities are carried at market value, and the market value is higher than cost, the difference between cost and market value is not disclosed as it cannot be determined without unreasonable expense.

The above market valuations do not take account of transactions entered into to hedge the value of the Group's investment securities. If these transactions were included, the market valuation of investment securities would be £11,144 million (1993: £12,319 million).

Investment securities:

	Cost	*Provisions*	*Book value*
	£m	**£m**	**£m**
At 1 January 1994	**12,280**	**(25)**	**12,255**
Exchange movements	**(78)**	**—**	**(78)**
Acquisitions	**10,452**	**—**	**10,452**
Disposals and amounts repaid	**(11,291)**	**—**	**(11,291)**
Transfers	**14**	**(7)**	**7**
Provisions made	**—**	**(1)**	**(1)**
Amortisation of discounts and premiums	**(49)**	**—**	**(49)**
At 31 December 1994	**11,328**	**(33)**	**11,295**

18 Equity shares

	1994		1993	
	Book value	*Market valuation*	*Book value*	*Market valuation*
	£m	**£m**	£m	£m
Investment securities				
— listed on a recognised UK exchange	**108**	**232**	14	39
— listed in Hong Kong	**144**	**459**	197	1,111
— listed elsewhere	**120**	**136**	92	118
— unlisted	**239**	**315**	144	202
	611	**1,142**	447	1,470
Other securities				
— listed on a recognised UK exchange	**216**		119	
— listed in Hong Kong	**175**		318	
— listed elsewhere	**628**		778	
— unlisted	**349**		288	
	1,979		1,950	

Where securities are carried at market value, and the market value is higher than cost, the difference between cost and market value is not disclosed as it cannot be determined without unreasonable expense.

Included in the above are 5,823,359 (1993: 2,567,972) shares in the Company held by subsidiary undertakings, as part of their insurance and retirement funds for the benefit of the policyholders and as equity market makers.

Investment securities:

	Cost	*Provisions*	*Book value*
	£m	**£m**	**£m**
At 1 January 1994	**532**	**(85)**	**447**
Exchange movements	**(7)**	**(1)**	**(8)**
Acquisitions	**103**	**—**	**103**
Disposals	**(134)**	**11**	**(123)**
Transfers from interests in associated undertakings	**70**	**—**	**70**
Transfers from other participating interests	**53**	**—**	**53**
Other transfers	**93**	**(10)**	**83**
Provisions made	**—**	**(14)**	**(14)**
At 31 December 1994	**710**	**(99)**	**611**

19 Interests in associated undertakings

	£m
At 1 January 1994	**556**
Exchange movements	**(18)**
Additions	**2**
Retained profits	**33**
Disposals	**(83)**
Transfer to equity shares	**(70)**
At 31 December 1994	**420**

19 Interests in associated undertakings *(continued)*

		1994	1993
		£m	£m
a	Shares in banks	**315**	309
	Other	**105**	247
		420	556
	Listed shares (all listed outside the UK and Hong Kong)	**235**	238
	Unlisted shares	**185**	318
		420	556

b The principal associated undertakings of the Group are:

	Accounts made up to	Country of incorporation	Principal activity	Group's interest in equity capital	Issued equity capital
The Cyprus Popular Bank Limited	31.12.94	Cyprus	Banking	22%	C£67m
Egyptian British Bank S.A.E.	31.12.94	Egypt	Banking	40%	E£60m
The Saudi British Bank	31.12.94	Saudi Arabia	Banking	40%	SR1,000m
UBAF Bank Limited	31.12.94	England	Banking	25%	US$81m (£32m fully paid, £5m nil paid
World Finance International Limited	30.6.94	Bermuda	Shipping	38%	US$58m
Kay Hian James Capel Holdings Limited	31.12.94	Singapore	Stockbroking	38%	S$33m
Banco Roberts SA	31.7.94	Argentina	Banking	30%	AP50m

All the above companies are owned by subsidiaries of the Company.

Part of the Group's shareholding in 3i Group plc was disposed of during the year and the remaining balance transferred to equity shares.

The principal countries of operation are the same as the countries of incorporation except for World Finance International Limited which operates world-wide.

c The associated undertakings listed above have no loan capital, except for The Cyprus Popular Bank Limited which has issued C£8 million, in which the Group has no interest, and UBAF Bank Limited which has issued US$29 million of subordinated unsecured loan stock and £10 million of subordinated loan stock in which the Group has a 25% and 13% interest respectively.

20 Other participating interests

	1994	1993
	£m	£m
Listed other than on a recognised UK exchange	**24**	12
Unlisted	**68**	122
	92	134
Market value of listed securities	**44**	29
Other participating interests in banks	**30**	26

Notes on the Accounts *(continued)*

20 Other participating interests *(continued)*

	Cost	*Provisions*	*Carrying value*
	£m	**£m**	**£m**
At 1 January 1994	**151**	**(17)**	**134**
Exchange movements	**(1)**	**—**	**(1)**
Additions	**15**	**—**	**15**
Disposals	**(2)**	**—**	**(2)**
Provisions made	**—**	**(1)**	**(1)**
Transfer to equity shares	**(53)**	**—**	**(53)**
At 31 December 1994	**110**	**(18)**	**92**

21 Tangible fixed assets

a *Group*	*Freehold land and buildings*	*Long leasehold land and buildings*	*Short leasehold land and buildings*	*Equipment, fixtures and fittings*	*Equipment on operating leases*	*Total*
	£m	**£m**	**£m**	**£m**	**£m**	**£m**
Cost or valuation at 1 January 1994	**1,149**	**2,654**	**647**	**1,761**	**344**	**6,555**
Exchange and other movements	**12**	**(132)**	**(18)**	**(40)**	**—**	**(178)**
Additions	**125**	**35**	**42**	**237**	**179**	**618**
Disposals	**(47)**	**(55)**	**(37)**	**(117)**	**(116)**	**(372)**
Reclassification	**23**	**(23)**	**—**	**—**	**—**	**—**
Permanent diminution in value of land and properties	**(32)**	**—**	**—**	**—**	**—**	**(32)**
Revaluation of investment properties	**—**	**195**	**—**	**—**	**—**	**195**
Cost or valuation at 31 December 1994	**1,230**	**2,674**	**634**	**1,841**	**407**	**6,786**
Accumulated depreciation at 1 January 1994	**(67)**	**(145)**	**(298)**	**(1,159)**	**(105)**	**(1,774)**
Exchange and other movements	**(1)**	**(5)**	**9**	**33**	**10**	**46**
Disposals	**7**	**7**	**21**	**98**	**68**	**201**
Charge for the year	**(16)**	**(26)**	**(39)**	**(178)**	**(83)**	**(342)**
Accumulated depreciation at 31 December 1994	**(77)**	**(169)**	**(307)**	**(1,206)**	**(110)**	**(1,869)**
Net book value at 31 December 1994	**1,153**	**2,505**	**327**	**635**	**297**	**4,917**
Net book value at 31 December 1993	1,082	2,509	349	602	239	4,781

b *Company*

	Freehold land and buildings
	£m
Cost or valuation at 1 January 1994 and at 31 December 1994	**11**

21 Tangible fixed assets *(continued)*

c *Valuations*

	Group		*Company*	
	1994	1993	**1994**	1993
	£m	£m	**£m**	£m
Cost or valuation of freehold and long and short leasehold land and buildings (excluding investment properties):				
At 1992 valuation, as adjusted for subsequent permanent diminution	**3,456**	3,721	**11**	11
At cost	**550**	365	**—**	—
	4,006	4,086	**11**	11
On the historical cost basis, freehold and long and short leasehold land and buildings would have been included as follows (excluding investment properties):				
Cost	**2,843**	2,860	**1**	1
Accumulated depreciation	**(392)**	(357)	**—**	—
	2,451	2,503	**1**	1

All freehold and long leasehold properties other than investment properties are revalued triennially. The last valuation was made as at 31 December 1992 and the results of the valuation were included in the balance sheet at that date.

d *Investment properties*

The valuation at which investment properties are included in Group tangible fixed assets, together with the net book value of these properties calculated under the historical cost basis, is as follows:

	1994		1993	
	At valuation	**At cost**	At valuation	At cost
	£m	**£m**	£m	£m
Freehold land and buildings	**3**	**3**	2	2
Long leaseholds	**529**	**52**	362	44
	532	**55**	364	46

Investment properties, which are valued annually, were valued on an open market value for existing use basis at 31 December 1994 and 1993 by professionally qualified internal staff. The surplus arising has been credited to reserves at 31 December 1994 after deduction of minority interests of £70 million. In 1993, the surplus arising on revaluation was not material.

The Company had no investment properties at 31 December 1994 or 1993.

e *Group properties leased to customers*

Group properties leased to customers, none of which was held by the Company, included £568 million at 31 December 1994 (1993: £407 million) let under operating leases, net of accumulated depreciation of £11 million (1993: £9 million).

f *Land and buildings occupied for own activities*

	1994	1993
	£m	£m
Net book value	**3,277**	2,918

There were no such assets in the Company at 31 December 1994 or 1993.

22 Investments

a

	Shares in Group undertakings	*Loans to Group undertakings*	*Other investments other than loans*	*Total*
	£m	**£m**	**£m**	**£m**
At 1 January 1994	**9,559**	**1,077**	**149**	**10,785**
Exchange movements	—	**(49)**	—	**(49)**
Additions	**51**	—	—	**51**
Repayments and redemptions	**(579)**	**(166)**	—	**(745)**
Disposals	**(51)**	—	—	**(51)**
Amortisation of discounts and premiums	—	—	**(2)**	**(2)**
Write-up of subsidiary undertakings to net asset value (Note 32)	**1,368**	—	—	**1,368**
At 31 December 1994	**10,348**	**862**	**147**	**11,357**

Shares in Group undertakings include £2,975 million (1993: £2,513 million) in respect of shares in banks, all of which are unlisted.

'Other investments other than loans' represents the Company's holdings of UK government stock.

	1994	1993
	£m	£m
On the historical cost basis, shares in Group undertakings would have been included as follows:		
Cost	**10,543**	11,122

There are no provisions for permanent diminution against these investments (1993: £ nil).

b The principal subsidiary undertakings of the Company are:

	Country of incorporation or registration	*Principal activity*	*Issued equity capital*
The British Bank of the Middle East	England	Banking	£100m
Carlingford Insurance Company Limited	Hong Kong	Insurance	HK$25m
Concord Leasing, Inc.	United States	Finance	—*
Forward Trust Limited	England	Finance	£265m
Gibbs Hartley Cooper Limited	England	Insurance	£3m
Guyerzeller Bank AG (75% owned)	Switzerland	Banking	SFr5m
Hang Seng Bank Limited (61.48% owned)	Hong Kong	Banking	HK$9,658m
The Hongkong and Shanghai Banking Corporation Limited	Hong Kong	Banking	HK$16,254m
HongkongBank of Australia Limited	Australia	Banking	A$500m
Hongkong Bank of Canada	Canada	Banking	C$75m
Hongkong Bank Malaysia Berhad	Malaysia	Banking	M$100m
HSBC Asset Management Asia Pacific Limited	Bahamas	Asset management	—*
HSBC Greenwell (formerly Greenwell Montagu Gilt-Edged)	England	Capital markets	£30m
HSBC Securities, Inc. (formerly Carroll McEntee & McGinley Inc.)	United States	Primary dealer in US government securities	—*

** Issued equity capital is less than US$1 million.*

22 Investments *(continued)*

	Country of incorporation or registration	*Principal activity*	*Issued equity capital*
James Capel & Co. Limited	England	Stockbroking	£125m
Marine Midland Bank	United States	Banking	US$185m
Midland Bank plc	England	Banking	£797m
Midland Life Limited (77.5% owned)	England	Insurance	£14m
Samuel Montagu & Co. Limited	England	Merchant banking	£112m
Trinkaus & Burkhardt KGaA (partnership limited by shares, 70% owned)	Germany	Banking	DM118m
Wardley Limited (from 7 February 1995, HSBC Investment Bank Asia Limited)	Hong Kong	Merchant banking	HK$770m
Wayfoong Finance Limited	Hong Kong	Finance	HK$300m

Details of all Group companies will be annexed to the next Annual Return of the Company.

Except where indicated otherwise, the above undertakings are wholly-owned subsidiaries and, except for Midland Bank plc, all are owned by subsidiaries of the Company. All the above make their accounts up to 31 December, except Hongkong Bank of Canada, whose accounts are made up to 31 October annually to comply with local regulations, and Midland Life Limited, whose accounts are made up to 31 August to avoid undue delay in the publication of the Group's accounts.

The principal countries of operation are the same as the countries of incorporation except for The British Bank of the Middle East which operates mainly in the Middle East. All the above subsidiaries are included in the consolidation.

23 Other assets

	1994	1993
	£m	£m
Gold bullion	**107**	216
Assets, including gains, resulting from off-balance-sheet interest rate and exchange rate contracts which are marked to market	**7,645**	8,426
Current taxation recoverable	**65**	60
Deferred taxation (Note 28a)	**34**	43
Other accounts	**3,871**	3,054
	11,722	11,799

24 Deposits by banks

	1994	1993
	£m	£m
Repayable on demand	**5,198**	4,807
With agreed maturity dates or periods of notice, by remaining maturity:		
— 3 months or less but not repayable on demand	**11,530**	20,023
— 1 year or less but over 3 months	**1,653**	2,228
— 5 years or less but over 1 year	**446**	1,038
— over 5 years	**300**	149
	19,127	28,245
Amounts include:		
Due to associated undertakings	**133**	144

Notes on the Accounts *(continued)*

25 Customer accounts

	1994 £m	1993 £m
Repayable on demand	**66,059**	67,757
With agreed maturity dates or periods of notice, by remaining maturity:		
— 3 months or less but not repayable on demand	**55,982**	56,144
— 1 year or less but over 3 months	**4,738**	4,019
— 5 years or less but over 1 year	**1,774**	891
— over 5 years	**154**	32
	128,707	128,843
Amounts include:		
Due to associated undertakings	**7**	18

26 Debt securities in issue

	1994 £m	1993 £m
Bonds and medium-term notes, by remaining maturity:		
— within 1 year	**24**	46
— between 1 and 2 years	**101**	29
— between 2 and 5 years	**126**	248
— over 5 years	**376**	203
	627	526
Other debt securities in issue, by remaining maturity:		
— 3 months or less	**4,030**	3,470
— 1 year or less but over 3 months	**2,501**	1,650
— 5 years or less but over 1 year	**1,586**	761
— over 5 years	**38**	37
	8,782	6,444

27 Other liabilities

	1994 £m	1993 £m
Short positions in securities:		
Treasury bills and other eligible bills	**1,011**	544
Debt securities		
— government securities	**2,045**	2,433
— other public sector securities	**52**	90
— other debt securities	**206**	84
Equity shares	**452**	149
	3,766	3,300
Liabilities, including losses, resulting from off-balance-sheet interest rate and exchange rate contracts which are marked to market	**7,357**	7,853
Current taxation	**831**	741
Obligations under finance leases	**128**	172
Proposed dividend	**495**	418
Insurance and retirement funds	**1,216**	1,376
Other liabilities	**4,718**	4,557
	18,511	18,417

27 Other liabilities *(continued)*

	1994 £m	1993 £m
Obligations under finance leases fall due as follows:		
— within 1 year	**57**	47
— between 1 and 5 years	**52**	106
— over 5 years	**19**	19
	128	172

28 Provisions for liabilities and charges

a *Deferred taxation*

i Deferred taxation is provided for in accordance with the Group's accounting policy in Note 2g.

	Group £m	*Company* £m
At 1 January 1994	**210**	**26**
Exchange and other movements	**3**	**(8)**
Reduction in advance corporation tax deferred tax asset arising from take-up of enhanced scrip dividend	**83**	**83**
(Credit)/charge to profit and loss account	**(7)**	**40**
At 31 December 1994	**289**	**141**

	Group		*Company*	
	1994 £m	1993 £m	**1994 £m**	1993 £m
Included in 'Provisions for liabilities and charges'	**323**	253	**141**	26
Included in 'Other assets' (Note 23)	**(34)**	(43)	**—**	—
Net deferred taxation provision	**289**	210	**141**	26
Comprising:				
Short-term timing differences	**22**	14	**—**	—
Leasing transactions	**222**	198	**—**	—
Relief for tax losses	**(5)**	(35)	**—**	—
Advance corporation tax carried forward in Midland	**(78)**	(80)	**—**	—
Advance corporation tax on dividends paid and proposed	**(124)**	(199)	**(124)**	(199)
Provision for additional UK tax on profit remittances from overseas	**200**	200	**200**	200
Other items	**52**	112	**65**	25
	289	210	**141**	26

Save as disclosed below there is no significant deferred taxation liability not provided for.

ii The distribution of the reserves of certain subsidiary and associated undertakings may give rise to additional tax liabilities. From 1 January 1993, the Company became UK tax resident and thereby became subject to UK corporation tax in respect of all its income (including dividends remitted from its non-UK resident subsidiary undertakings) and chargeable gains. A provision for a potential UK tax charge of £200 million was established upon the acquisition of Midland to reflect the expected additional UK tax cost of remitting dividends.

iii No provision is made for deferred taxation on revalued premises. The Directors are of the opinion that, in respect of properties occupied for the purposes of the Group's business, the likelihood of a material taxation liability arising is remote and no useful purpose would be served by attempting to quantify it. In respect of investment and other properties which have been revalued, no material taxation liability is judged likely to arise in the foreseeable future under management's current intentions for these properties.

28 Provisions for liabilities and charges *(continued)*

iv At 31 December 1994, there were potential future tax benefits of approximately £310 million (1993: £220 million) in respect of trading losses and advance corporation tax carried forward by subsidiary undertakings which have not been recognised because recoverability of the potential benefits is not considered certain.

v Unprovided deferred tax in respect of leasing transactions carried out by Midland totalled £63 million as at 31 December 1994 (1993: £87 million).

b *Other provisions for liabilities and charges*

	Provisons for pension and other post-retirement obligations	*Provisions for contingent liabilities and commitments*	*Other provisions*	*Total*
	£m	£m	£m	£m
At 1 January 1994	81	125	143	349
Exchange movements	1	—	(1)	—
Charges against profits	43	65	8	116
Provisions utilised	(24)	(51)	(34)	(109)
Other movements	(1)	(8)	1	(8)
At 31 December 1994	100	131	117	348

Acquisition provisions reflecting the restructuring costs of achieving the synergy benefits of the merger with Midland were established in 1992. Of these provisions, £40 million was utilised during the year and the unutilised balance of £70 million (1993: £110 million) is included in 'Other provisions' in the table above. The unutilised balance relates mainly to the cost of surplus space arising as a result of the merger.

None of the above provisions relates to the Company (1993: £ nil).

29 Subordinated liabilities

	1994 £m	1993 £m
Undated subordinated loan capital:		
— the Company	—	—
— other Group	1,761	1,859
	1,761	1,859
Dated subordinated loan capital:		
— the Company	819	827
— other Group	2,629	2,501
	3,448	3,328
Total subordinated liabilities:		
— the Company	819	827
— other Group	4,390	4,360
	5,209	5,187
Dated subordinated loan capital is repayable:		
— within 1 year	4	85
— between 1 and 2 years	163	4
— between 2 and 5 years	736	614
— over 5 years	2,545	2,625
	3,448	3,328

29 Subordinated liabilities *(continued)*

The total subordinated borrowings of the Company are as follows:

		1994 £m	1993 £m
£413m	11.69% subordinated bonds 2002	**413**	413
£250m	9.875% subordinated bonds 2018	**246**	245
US$250m	Subordinated collared floating rate notes 2008	**160**	169
		819	827
Amounts owed to Group undertakings:			
US$350m	7.525% subordinated loan 2003 — HSBC Finance Nederland BV	**223**	235
		1,042	1,062

At 31 December 1994, the following other Group subordinated borrowings of £100 million or over were:

		1994 £m	1993 £m
US$1,200m	Primary capital subordinated undated floating rate notes	**768**	812
US$750m	Undated floating rate primary capital notes	**480**	506
US$500m	Undated floating rate primary capital notes	**320**	337
US$400m	8.625% subordinated notes 2004*	**253**	—
£250m	Subordinated unsecured floating rate notes 2001	**250**	250
HK$3,000m	Subordinated collared floating rate notes 2003	**248**	263
US$350m	7.4% subordinated guaranteed notes 2003	**224**	237
US$300m	Undated floating rate primary capital notes (Series 3)	**192**	203
US$200m	Guaranteed floating rate notes 1999	**128**	135
US$200m	Floating rate subordinated notes 2000 (1993: US$157m)	**128**	105
DM300m	Guaranteed floating rate notes 1986/98	**124**	117
£100m	14% subordinated unsecured loan stock 2002/07	**100**	100
	Other subordinated liabilities less than £100m	**1,175**	1,295
		4,390	4,360

* *The proceeds of the issue of 8.625% subordinated notes 2004 during the year were used to support the development of Midland Bank plc and to strengthen further Midland's capital base.*

Generally, subordinated loan capital is repayable at par on maturity but some is repayable prior to maturity at the option of the borrower, in certain cases at a premium over par. Interest rates on the floating rate loan capital are related to Interbank Offered Rates. On the remaining subordinated loan capital, interest is payable at fixed rates of between 5% and 14%.

30 Minority interests — non-equity

Preference shares issued by subsidiary undertakings:

		1994 £m	1993 £m
US$98m	Perpetual preference shares	**63**	66
US$250m	Non-cumulative preference shares	**156**	164
		219	230

Notes on the Accounts *(continued)*

31 Called up share capital

Authorised:

The authorised ordinary share capital of the Company at 31 December 1994 and 1993 is HK$20,000 million divided into 2,000 million ordinary shares of HK$10 each, £1,125 million divided into 1,500 million ordinary shares of 75p each, and £301,500 divided into 301,500 non-voting deferred shares of £1 each; in addition, at 31 December 1994 and 1993, the authorised preference share capital of the Company is £500 million divided into 500 million non-cumulative preference shares of £1 each.

	HK$10 *shares* *Number*	75p *shares* *Number*	£m
Issued:			
At 1 January 1994	1,706,829,463	821,296,686	**2,111**
Shares issued under option scheme	—	3,849,902	**3**
Shares issued in lieu of dividends	47,346,646	26,448,048	**60**
Exchange movements	—	—	**(84)**
At 31 December 1994	1,754,176,109	851,594,636	**2,090**

The 301,500 non-voting deferred shares are held by a subsidiary undertaking of the Company.

Options outstanding to subscribe for the Company's ordinary shares of 75p each under the Group's executive and savings-related share option schemes and Midland's executive and savings-related share option schemes are as follows:

	Number of shares	*Period of exercise*	*Price*
1994	**36,295,570**	**1995 to 2004**	**£1.1843 to £8.5127**
1993	21,734,644	1994 to 2003	£1.1843 to £7.2184

32 Reserves

	Group	*Company*	*Associated undertakings*
	£m	**£m**	**£m**
Share premium account:			
At 1 January 1994	**378**	**378**	—
Shares issued under option scheme	**5**	**5**	—
Shares issued in lieu of dividends and associated issue costs	**(64)**	**(64)**	—
At 31 December 1994	**319**	**319**	—
Reserves:			
— Merger reserve			
At 1 January 1994 and 31 December 1994	**148**	—	—
Revaluation reserve:			
— Investment property revaluation reserve			
At 1 January 1994	**195**	—	—
Exchange and other movements	**(5)**	—	—
Unrealised surplus on revaluation of land and buildings	**125**	—	—
At 31 December 1994	**315**	—	—

32 Reserves *(continued)*

	Group	*Company*	*Associated undertakings*
	£m	**£m**	**£m**
— Revaluation reserve			
At 1 January 1994	**1,226**	**4,003**	**—**
Exchange and other movements	**(22)**	**80**	**—**
Realisation on disposal of properties	**(9)**	**—**	**—**
Permanent diminution in value of premises	**(32)**	**—**	**—**
Net increase in attributable net assets of subsidiary undertakings	**—**	**1,368**	**—**
At 31 December 1994	**1,163**	**5,451**	**—**
Total revaluation reserve	**1,478**	**5,451**	**—**
Profit and loss account:			
At 1 January 1994	**5,276**	**2,842**	**145**
Exchange and other movements	**(252)**	**—**	**31**
Retained profit/(loss) for the year	**1,350**	**(284)**	**33**
Realisation on disposal of properties	**9**	**—**	**—**
Partial disposal and reclassification of residual investment in associated undertaking	**—**	**—**	**(128)**
Arising on shares issued in lieu of dividends	**372**	**372**	**—**
At 31 December 1994	**6,755**	**2,930**	**81**

Goodwill amounting to £2,154 million (1993: £2,154 million) has been charged against reserves in current and prior years in respect of acquisitions.

Many of the Group's banking subsidiary undertakings operate under local regulatory jurisdictions which could potentially restrict the amount of reserves which can be remitted to the Company in order to maintain local regulatory capital ratios. In addition, as stated in Note 28 above, the remittance of reserves may result in further taxation liabilities.

33 Analysis of total assets and total liabilities

	1994	1993
	£m	£m
a *Assets and liabilities denominated in foreign currency*		
Denominated in sterling	**59,847**	52,772
Denominated in currencies other than sterling	**141,671**	154,675
Total assets	**201,518**	207,447
Denominated in sterling	**66,021**	58,162
Denominated in currencies other than sterling	**135,497**	149,285
Total liabilities	**201,518**	207,447

b *Assets subject to sale and repurchase transactions*	**1994**	1993
	£m	£m
Total assets subject to sale and repurchase transactions	**1,833**	2,992

c *Assets leased to customers*	**1994**	1993
	£m	£m
Loans and advances to customers	**3,994**	4,889
Tangible fixed assets — equipment on operating leases (Note 21a)	**297**	239
	4,291	5,128

33 Analysis of total assets and total liabilities *(continued)*

The cost of assets acquired during 1994 for letting to customers under finance leases and hire purchase contracts by the Group amounted to £1,902 million (1993: £1,927 million).

d *Assets charged as security for liabilities*

The Group has pledged assets as security for liabilities included under the following headings:

	Amount of liability secured	
	1994	1993
	£m	£m
Deposits by banks	**1,312**	1,706
Customer accounts	**1,808**	2,199
Debt securities in issue	**517**	136
Other liabilities	**911**	950
	4,548	4,991

The amount of assets pledged to secure these amounts is £7,134 million (1993: £4,699 million) and is mainly made up of items included in 'Loans and advances to banks' (£1,002 million; 1993: £1,657 million) and 'Debt securities' (£4,512 million; 1993: £2,423 million).

e *Restatement of balances for FRS 5*

The effect of restating 1993 balances to reflect the implementation of FRS 5 is set out below:

	1993	1993
	£m	£m
Total assets previously reported	206,050	
Total liabilities previously reported		206,050
Loans and advances to banks (Note 2b)	1,997	
Loans and advances to customers (Note 2b)	(600)	
Deposits by banks		1,997
Customer accounts		(1,403)
Other liabilities		803
Restated total assets	207,447	
Restated total liabilities		207,447

34 Memorandum items

	1994			1993		
	Contract amount	*Credit equivalent amount*	*Risk-weighted amount*	*Contract amount*	*Credit equivalent amount*	*Risk-weighted amount*
a *Group*	**£m**	**£m**	**£m**	£m	£m	£m
Contingent liabilities:						
Acceptances and endorsements	**1,325**	**911**	**869**	1,398	992	913
Guarantees and assets pledged as collateral security						
— guarantees and irrevocable letters of credit	**11,893**	**9,395**	**6,822**	10,733	8,480	6,072
Other contingent liabilities	**183**	**—**	**—**	352	222	216
	13,401	**10,306**	**7,691**	12,483	9,694	7,201

34 Memorandum items *(continued)*

	1994			1993		
	Contract amount	*Credit equivalent amount*	*Risk-weighted amount*	*Contract amount*	*Credit equivalent amount*	*Risk-weighted amount*
	£m	**£m**	**£m**	£m	£m	£m
Commitments:						
Documentary credits and short-term trade-related transactions	**5,464**	**1,389**	**1,062**	4,878	1,076	877
Forward asset purchases and forward forward deposits placed	**161**	**161**	**52**	187	187	97
Undrawn note issuing and revolving underwriting facilities	**300**	**150**	**150**	1,052	526	526
Undrawn formal standby facilities, credit lines and other commitments to lend:						
— over 1 year	**12,610**	**6,305**	**5,040**	13,268	6,634	5,305
— 1 year and under	**42,362**	**—**	**—**	38,422	—	—
	60,897	**8,005**	**6,304**	57,807	8,423	6,805
Exchange rate contracts	**302,302**	**6,114**	**1,512**	279,244	5,343	1,343
Interest rate contracts	**745,971**	**5,166**	**1,225**	554,809	5,825	1,430

The table above gives the nominal principal amounts, credit equivalent amounts and risk-weighted amounts of off-balance-sheet transactions. The credit equivalent amounts are calculated for the purposes of deriving the risk-weighted amounts. These are assessed in accordance with the Bank of England's guidelines which implement the Basle agreement on capital adequacy and depend on the status of the counterparty and the maturity characteristics. The risk weights used range from 0% to 100% for contingent liabilities and commitments, and from 0% to 50% for exchange rate and interest rate contracts.

Contingent liabilities and commitments are credit-related instruments which include acceptances, letters of credit, guarantees and commitments to extend credit. The contractual amounts represent the amounts at risk should the contract be fully drawn upon and the client default. Since a significant portion of guarantees and commitments is expected to expire without being drawn upon, the total of the contract amounts is not representative of future liquidity requirements.

Off-balance-sheet financial instruments arise from futures, forward, swap and option transactions undertaken by the Group in the foreign exchange, interest rate and equity markets.

Included in the above table are £293,345 million (1993: £272,427 million) contract amount of exchange rate contracts and £668,962 million (1993: £425,092 million) contract amount of interest rate contracts which were made for dealing purposes. The remaining exchange and interest rate contracts were made for non-dealing purposes, i.e. to hedge risk, or as part of the management of asset and liability portfolios, either directly with the market-place or indirectly through Group counterparties.

The notional or contractual amounts of these instruments indicate the volume of transactions outstanding at the balance sheet date; they do not represent amounts at risk.

34 Memorandum items *(continued)*

	1994 £m	1993 £m
Replacement cost of contracts:		
— exchange rate contracts	**3,514**	3,038
— interest rate contracts	**4,697**	5,564
	8,211	8,602

Replacement cost of contracts represents the mark-to-market assets on all contracts with a positive value. The comparative figures have been restated to be consistent with the basis used for the balance sheet presentation of trading contracts. Previously, contracts were excluded where they were not risk-weighted for Bank of England regulatory purposes.

Replacement cost is a close approximation of the credit risk for these contracts as at the balance sheet date. Credit risk is measured internally as the sum of positive mark-to-market values and an estimate for the future fluctuation risk, using a future risk factor.

b *Company*

The Company had contingent liabilities of £7 million (1993: £377 million). In addition, the Company enters into guarantees and letters of support on behalf of other Group undertakings in the normal course of business.

35 Reconciliation of operating profit to net cash flow from operating activities

	1994 £m	1993 £m
Operating profit	**2,714**	2,202
Change in prepayments and accrued income	**308**	(150)
Change in accruals and deferred income	**(195)**	236
Interest paid on finance leases and similar hire purchase contracts	**15**	21
Interest on loan capital	**298**	350
Depreciation and amortisation	**342**	320
Provisions for bad and doubtful debts	**275**	1,158
Loans written off net of recoveries	**(1,053)**	(1,344)
Provisions for liabilities and charges	**116**	273
Provisions utilised	**(109)**	(319)
Amounts written off fixed asset investments	**6**	32
Income receivable on investment securities	**(703)**	(797)
Net cash flow from trading activities	**2,014**	1,982
Change in items in the course of collection from other banks	**287**	(146)
Change in treasury bills and other eligible bills	**(1,901)**	639
Change in loans and advances to banks	**1,440**	715
Change in loans and advances to customers	**(367)**	(4,415)
Change in other securities	**4,189**	(6,233)
Change in other assets	**(49)**	1,199
Change in deposits by banks	**(9,118)**	7,108
Change in customer accounts	**(136)**	10,317
Change in items in the course of transmission to other banks	**(417)**	162
Change in debt securities in issue	**2,338**	601
Change in other liabilities	**(63)**	(682)
Elimination of exchange differences	**534**	(237)
Net cash (outflow)/inflow from operating activities	**(1,249)**	11,010

36 Changes in financing during the year

	Loan capital	Preference shares*	Ordinary shares	Share premium
	£m	**£m**	**£m**	**£m**
Balance at 1 January 1994	**5,187**	**230**	**2,111**	**378**
Shares issued in lieu of dividends	**—**	**—**	**60**	**(64)**
Issued during the year	**420**	**—**	**3**	**5**
Repaid during the year	**(301)**	**—**	**—**	**—**
Net cash inflow from financing	**119**	**—**	**3**	**5**
Exchange and other movements	**(97)**	**(11)**	**(84)**	**—**
Balance at 31 December 1994	**5,209**	**219**	**2,090**	**319**

** Preference shares in issue are in subsidiary undertakings (Note 30).*

37 Analysis of cash and cash equivalents

a *Deposits required by government regulations and included in the consolidated balance sheet*

	1994	1993
	£m	£m
Loans and advances to banks	**883**	559
Treasury bills	**101**	146
	984	705

b *Changes in cash and cash equivalents during the year*

	1994	1993
	£m	£m
Balance at 1 January	**35,576**	28,822
Net cash (outflow)/inflow before the effect of foreign exchange movements	**(799)**	6,411
Effect of foreign exchange movements	**(1,028)**	343
Balance at 31 December	**33,749**	35,576

c *Analysis of the balances of cash and cash equivalents as classified in the consolidated balance sheet*

	1994	1993
	£m	£m
Cash and balances at central banks	**1,829**	1,622
Treasury bills and other eligible bills	**3,109**	2,800
Loans and advances to banks	**27,192**	29,696
Other assets	**107**	216
Debt securities	**1,512**	1,242
	33,749	35,576

38 Litigation

Proceedings which were initiated by British & Commonwealth Holdings plc against Samuel Montagu & Co. Limited ('Samuel Montagu') in connection with the proposed purchase in 1987 by Quadrex Holdings Inc. of the wholesale broking division of Mercantile House Holdings plc resulted in a judgement of approximately £176 million being awarded against Samuel Montagu in 1993, who have appealed against this judgement. These accounts reflect full provision in respect of this judgement after charging £125 million during 1993 (Note 5).

The Group, through a number of its subsidiary undertakings, is named in and is defending other legal actions in various jurisdictions arising from its normal business. No material adverse impact on the financial position of the Group is expected to arise from these proceedings.

39 Capital commitments

	1994	1993
	£m	£m
Expenditure contracted for	**169**	126
Expenditure authorised by Directors but not contracted for	**104**	34
	273	160

Included in the above is £ nil (1993: £6 million) of expenditure authorised by Directors but not contracted for in respect of the Company.

40 Lease commitments

At the year-end, annual commitments under non-cancellable operating leases were:

	1994	1993
	£m	£m
Leasehold land and buildings		
Operating leases which expire:		
— within 1 year	**26**	83
— between 1 and 5 years	**98**	108
— over 5 years	**145**	148
	269	339
Equipment		
Operating leases which expire:		
— within 1 year	**2**	13
— between 1 and 5 years	**4**	13
	6	26

The Company had no commitments under operating leases at 31 December 1994 (1993: none).

41 Segmental analysis

a *By geographic region*

As the Group is not required to disclose turnover, no segmental analysis of turnover is included. Turnover of non-banking businesses is included in other operating income above. Common costs are included in segments on the basis of the actual recharges made. The allocation of earnings reflects the benefit of shareholders' funds to the extent that these are actually allocated to businesses in the segment by way of intra-Group capital and funding structures.

Geographical information has been classified by the location of the principal operations of the subsidiary undertaking, or in the case of HongkongBank, Midland and The British Bank of the Middle East operations, by the location of the branch responsible for reporting the results or for advancing the funds. Due to the nature of the Group structure, the analysis of profits and net assets shown below includes intra-Group items between geographic regions.

Total assets:	**At 31 December 1994**		At 31 December 1993	
	£m	**%**	£m	%
UK	**74,197**	**37.7**	81,794	40.4
Continental Europe	**11,006**	**5.6**	9,390	4.6
Hong Kong	**59,723**	**30.4**	59,193	29.3
Rest of Asia-Pacific	**23,572**	**12.0**	20,730	10.3
Americas	**28,014**	**14.3**	31,186	15.4
	196,512	**100.0**	202,293	100.0
Add: Hong Kong Government certificates of indebtedness	**5,006**		5,154	
Total assets	**201,518**		207,447	

41 Segmental analysis *(continued)*

Net assets:

	At 31 December 1994		At 31 December 1993	
	£m	%	£m	%
UK	**3,837**	**35.5**	3,083	33.0
Continental Europe	**568**	**5.3**	560	6.0
Hong Kong	**4,193**	**38.9**	3,848	41.2
Rest of Asia-Pacific	**926**	**8.6**	657	7.1
Americas	**1,266**	**11.7**	1,186	12.7
Total net assets	**10,790**	**100.0**	9,334	100.0

Profit on ordinary activities before tax:

	UK	*Continental Europe*	*Hong Kong*	*Rest of Asia-Pacific*	*Americas*	*Total*
Year ended 31 December 1994	**£m**	**£m**	**£m**	**£m**	**£m**	**£m**
Interest receivable	**4,433**	**624**	**3,526**	**1,376**	**1,648**	**11,607**
Interest payable	**(2,679)**	**(491)**	**(2,095)**	**(874)**	**(871)**	**(7,010)**
Net interest income	**1,754**	**133**	**1,431**	**502**	**777**	**4,597**
Dividend income	**16**	**5**	**37**	**3**	**9**	**70**
Fees and commissions receivable	**1,324**	**132**	**503**	**257**	**288**	**2,504**
Fees and commissions payable	**(49)**	**(12)**	**(29)**	**(34)**	**(49)**	**(173)**
Dealing profits	**45**	**27**	**86**	**95**	**8**	**261**
Other operating income	**274**	**9**	**201**	**24**	**63**	**571**
Operating income	**3,364**	**294**	**2,229**	**847**	**1,096**	**7,830**
Operating expenses	**(2,412)**	**(197)**	**(956)**	**(395)**	**(810)**	**(4,770)**
Operating profit before provisions	**952**	**97**	**1,273**	**452**	**286**	**3,060**
Provisions for bad and doubtful debts	**(99)**	**(11)**	**(22)**	**(8)**	**(135)**	**(275)**
Provisions for contingent liabilities and commitments	**(47)**	**—**	**(3)**	**(15)**	**—**	**(65)**
Amounts written off fixed asset investments	**—**	**(1)**	**(3)**	**(1)**	**(1)**	**(6)**
Operating profit	**806**	**85**	**1,245**	**428**	**150**	**2,714**
Profit on disposal of fixed assets and investments	**145**	**5**	**185**	**11**	**20**	**366**
Income from associated undertakings	**31**	**4**	**5**	**39**	**7**	**86**
Profit on ordinary activities before tax	**982**	**94**	**1,435**	**478**	**177**	**3,166**

41 Segmental analysis *(continued)*

Year ended 31 December 1993	UK £m	Continental Europe £m	Hong Kong £m	Rest of Asia-Pacific £m	Americas £m	Total £m
Interest receivable	5,003	693	3,140	1,089	1,606	11,531
Interest payable	(3,245)	(559)	(1,791)	(652)	(846)	(7,093)
Net interest income	1,758	134	1,349	437	760	4,438
Dividend income	20	2	37	6	7	72
Fees and commissions receivable	1,235	129	469	203	284	2,320
Fees and commissions payable	(47)	(32)	(32)	(5)	(204)	(320)
Dealing profits	615	112	175	103	84	1,089
Other operating income	188	(5)	307	187	100	777
Operating income	3,769	340	2,305	931	1,031	8,376
Operating expenses	(2,288)	(212)	(899)	(530)	(859)	(4,788)
Operating profit before provisions	1,481	128	1,406	401	172	3,588
Provisions for bad and doubtful debts	(647)	(131)	(81)	(44)	(255)	(1,158)
Provisions for contingent liabilities and commitments	(176)	(1)	(16)	(3)	—	(196)
Amounts written off fixed asset investments	(18)	(8)	(2)	—	(4)	(32)
Operating profit/(loss)	640	(12)	1,307	354	(87)	2,202
Profit on disposal of fixed assets and investments	52	10	208	8	9	287
Income from associated undertakings	26	4	8	46	11	95
Profit/(loss) on ordinary activities before tax	718	2	1,523	408	(67)	2,584

Total interest receivable and total interest payable include intra-Group interest of £832 million (1993: £852 million). Other operating income and operating expenses include intra-Group items of £206 million (1993: £362 million).

b *By class of business*

	Commercial banking		Investment banking		Total	
	1994 £m	1993 £m	**1994 £m**	1993 £m	**1994 £m**	1993 £m
Segment result before exceptional items	**2,937**	2,478	**229**	231	**3,166**	2,709
Provision in respect of British & Commonwealth Holdings plc litigation (Note 38)	—	—	—	(125)	—	(125)
Profit on ordinary activities before tax	**2,937**	2,478	**229**	106	**3,166**	2,584
Total assets	**192,970**	194,849	**8,548**	12,598	**201,518**	207,447
Net assets	**10,110**	8,551	**680**	783	**10,790**	9,334

Certain operations included in the investment banking segment in 1993 are no longer managed as part of this grouping. Comparative data have therefore been restated.

42 Transactions, arrangements and agreements involving Directors and others

Particulars of transactions, arrangements and agreements entered into by subsidiary undertakings of the Company with Directors and connected persons and companies controlled by them and with officers of the Company disclosed pursuant to Section 232 of the Companies Act 1985:

	1994		1993	
	Number	**£m**	Number	£m
Directors and connected persons and companies controlled by them:				
Loans and credit card transactions, including £52,000 in credit card transactions (1993: £47,000) and £9,347,000 in guarantees (1993: £ nil)	**54**	**178**	50	194
Officers:				
Loans and credit card transactions, including £26,000 in credit card transactions (1993: £24,000)	**17**	**3**	12	4

Particulars of Directors' transactions are recorded in a register held at the Registered Office of the Company which is available for inspection by members.

43 Foreign currency amounts

The Hong Kong and United States dollar figures shown in the consolidated profit and loss account and the balance sheets are for information only. They are translated from sterling at the average rates of exchange for the year ended 31 December 1994 and the closing rate at that date respectively. These were as follows:

	Average rate	*Closing rate*
£1.00 = HK$	11.853	12.085
£1.00 = US$	1.534	1.562

44 UK and Hong Kong accounting requirements

Where UK accounting requirements differ materially from those in Hong Kong Statements of Standard Accounting Practice, these relate to more detailed disclosures and prescribed formats and there were no material conflicts in accounting treatment. In each case, the UK requirement is the more prescriptive. The main differences in accounting requirements relate to changes to the UK Companies Act 1985 and to pronouncements of the UK Accounting Standards Board and Urgent Issues Task Force which came into effect for financial statements for years ended subsequent to 1992.

45 Approval of accounts

These accounts were approved by the Board of Directors on 27 February 1995.

Statement of Directors' Responsibilities in Relation to Financial Statements

The following statement, which should be read in conjunction with the Auditors' statement of their responsibilities set out in their report below, is made with a view to distinguishing for shareholders the respective responsibilities of the Directors and of the Auditors in relation to the financial statements.

The Directors are required by the Companies Act 1985 to prepare financial statements for each financial year which give a true and fair view of the state of affairs of the Company and its subsidiary undertakings as at the end of the financial year and of the profit or loss for the financial year. The Directors are required to prepare these financial statements on the going concern basis unless it is not appropriate. Since the Directors are satisfied that the Group has the resources to continue in business for the foreseeable future, the financial statements continue to be prepared on the going concern basis.

The Directors consider that in preparing the financial statements on pages 43 to 79, the Company has used appropriate accounting policies, consistently applied, save as disclosed in the 'Notes on the Accounts', and supported by reasonable and prudent judgements and estimates, and that all accounting standards which they consider to be applicable have been followed.

The Directors have responsibility for ensuring that the Company keeps accounting records which disclose with reasonable accuracy the financial position of the Company and which enable them to ensure that the financial statements comply with the Companies Act 1985.

The Directors have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

On behalf of the Board
R G Barber, *Secretary*

27 February 1995

Report of the Auditors, KPMG, to the Members of HSBC Holdings plc

We have audited the financial statements on pages 43 to 79.

Respective responsibilities of Directors and Auditors
As described above, the Company's Directors are responsible for the preparation of financial statements. It is our responsibility to form an independent opinion, based on our audit, on those statements and to report our opinion to you.

Basis of opinion
We conducted our audit in accordance with Auditing Standards issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the Directors in the preparation of the financial statements, and of whether the accounting policies are appropriate to the Group's circumstances, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion we also evaluated the overall adequacy of the presentation of information in the financial statements.

Opinion
In our opinion the financial statements give a true and fair view of the state of affairs of the Company and of the Group as at 31 December 1994 and of the profit of the Group for the year then ended and have been properly prepared in accordance with the Companies Act 1985.

KPMG
Chartered Accountants/Registered Auditors
London

27 February 1995

Taxation of Shares and Dividends

1. Cash Dividends

Since 1 January 1993, when the Company became UK resident for UK taxation purposes, HSBC Holdings plc has had to account to the UK Inland Revenue for advance corporation tax when the Company pays a dividend.

For individual shareholders who are resident in the United Kingdom for taxation purposes and liable to UK income tax at the basic rate, no further tax liability will arise. Individual shareholders who are liable to UK income tax at the higher rate of 40 per cent will be taxed on the dividend, including the tax credit of 20 per cent. The tax credit will then be available for set-off against the higher rate liability. Individual UK-resident shareholders whose income falls within the lower rate band of income tax charged at 20 per cent will not be entitled to any tax credit repayment. Other UK-resident shareholders who are exempt from tax on their investment income will be entitled to repayment by the UK Inland Revenue of the tax credit in respect of dividends at the rate of 20 per cent.

Non-UK-resident shareholders are generally not entitled to any payment of the tax credit in respect of any dividend received. However, some shareholders who are not resident in the United Kingdom may be entitled to a cash payment from the Inland Revenue of a proportion of the tax credit in respect of dividends received. Such entitlement depends in general either upon the provisions of any double taxation agreement between the country of residence and the United Kingdom, or upon the shareholder being a Commonwealth (including Hong Kong) citizen or a citizen of the Republic of Ireland.

Dividends paid by HSBC Holdings plc are generally not subject to tax in Hong Kong.

2. Scrip Dividends

Information on the taxation consequences of the HSBC Holdings plc enhanced scrip dividend offered in lieu of the 1993 final dividend was set out in the Chairman's letter to shareholders of 8 April 1994. Information on the taxation consequences of the HSBC Holdings plc scrip dividend offered in lieu of the 1994 interim dividend was set out in the Secretary's letter to shareholders of 29 September 1994. Shareholders should contact their usual professional advisers to obtain further information.

The price of the Company's shares on the first day of dealing (9 June 1994), as agreed with the UK Inland Revenue for shares issued under the enhanced scrip dividend offer, both for income and capital gains tax purposes, is as follows:

75p ordinary shares — £7.105215	HK$10 ordinary shares — £7.315000

As regards the 1994 interim dividend scrip issue, the market value of the Company's new ordinary shares on the first day of dealing (21 November 1994) was not substantially different from the cash dividend forgone and, accordingly, the price of both classes of the Company's shares for income and capital gains tax purposes is £7.65.

3. UK Capital Gains Tax

The computation of the capital gains tax liability arising on disposals of shares in the Company by shareholders subject to UK capital gains tax can be complex, partly dependent on whether the shares were purchased since April 1991, acquired in April 1991 in exchange for shares in The Hongkong and Shanghai Banking Corporation Limited, or acquired in July 1992 in acceptance of the offer for shares in Midland Bank plc.

Whilst it is not possible to give specific guidance on the tax calculation, it may be helpful to note that the market value of the relevant shares as at 31 March 1982 (before any adjustment to take account of subsequent rights and capitalisation issues) was:

The Hongkong and Shanghai Banking Corporation Limited	£1.36
Midland Bank plc	£3.23

For capital gains tax purposes, the acquisition cost for ordinary shares is adjusted to take account of subsequent rights and capitalisation issues. Further adjustments may be necessary where a shareholder has chosen to receive shares instead of cash dividends. Any capital gain arising on a disposal will also be adjusted to take account of indexation allowance.

If in doubt, shareholders are recommended to consult their professional advisers.

International Network

Services are provided by more than 3,000 offices in 68 countries:

Asia-Pacific	*Offices*		*Offices*
Australia	*32*	Malaysia	*46*
Brunei Darussalam	*11*	Myanmar	*1*
China	*13*	New Zealand	*3*
Cook Islands	*2*	Pakistan	*4*
Hong Kong	*411*	Philippines	*3*
India	*25*	Singapore	*26*
Indonesia	*7*	Sri Lanka	*5*
Japan	*10*	Taiwan	*6*
Korea, Republic of	*4*	Thailand	*4*
Macau	*7*	Vietnam	*2*
Europe			
Channel Islands	*26*	Luxembourg	*2*
Czech Republic	*1*	Netherlands	*1*
Finland	*1*	Poland	*1*
France	*3*	Russia	*1*
Germany	*14*	Spain	*2*
Greece	*4*	Sweden	*3*
Hungary	*1*	Switzerland	*5*
Ireland	*2*	Turkey	*1*
Isle of Man	*4*	United Kingdom	*1,823*
Italy	*1*		
Middle East and Africa			
Angola	*2*	Mauritius	*11*
Bahrain	*6*	Oman	*4*
Cyprus	*136*	Palestinian Autonomous Area	*1*
Egypt	*4*	Qatar	*2*
Ghana	*1*	Saudi Arabia	*56*
Jordan	*5*	South Africa	*1*
Kenya	*1*	United Arab Emirates	*13*
Lebanon	*4*	Zambia	*1*
Americas			
Argentina	*32*	Colombia	*2*
Bahamas	*10*	Guam	*1*
Bermuda	*2*	Mexico	*4*
Brazil	*4*	Panama	*3*
Canada	*116*	United States of America	*384*
Cayman Islands	*4*	Venezuela	*1*
Chile	*5*		

Principal Offices

HSBC Holdings plc
UNITED KINGDOM
Group Head Office
10 Lower Thames Street
London EC3R 6AE
Telephone: 0171-260 0500
Facsimile: 0171-260 0501

COMMERCIAL BANKING

Banco Roberts S.A.
ARGENTINA
25 de Mayo 258
1002 Buenos Aires
Telephone: 1-334 3968
Facsimile: 1-334 6404

The British Bank of the Middle East
CHANNEL ISLANDS
Head Office
1 Grenville Street, St Helier
Jersey JE2 4UF
Telephone: 01534-606511
Facsimile: 01534-606149

The Cyprus Popular Bank Limited
CYPRUS
Popular Bank Building
39 Archbishop Makarios III Avenue
Nicosia
Telephone: (02) 450000
Facsimile: (02) 453355

Egyptian British Bank S.A.E.
EGYPT
Abu El Feda Building
3 Abu El Feda Street, Zamalek, Cairo
Telephone: (2) 3404849, 3409186
Facsimile: (2) 3414010

Hang Seng Bank Limited
HONG KONG
Head Office
83 Des Voeux Road Central
Telephone: 2825 5111
Facsimile: 2845 9301

The Hongkong and Shanghai Banking Corporation Limited
HONG KONG
Head Office
1 Queen's Road Central
Telephone: 2822 1111
Facsimile: 2810 1112

Hongkong Bank Malaysia Berhad
MALAYSIA
Head Office
2 Leboh Ampang
50100 Kuala Lumpur
Telephone: (03) 2300744
Facsimile: (03) 2301146

HongkongBank of Australia Limited
AUSTRALIA
Level 10, 1 O'Connell Street
Sydney, NSW 2000
Telephone: (02) 255-2888
Facsimile: (02) 255-2332

Hongkong Bank of Canada
CANADA
Head Office
Suite 300, 885 West Georgia Street
Vancouver, BC V6C 3E9
Telephone: (604) 685-1000
Facsimile: (604) 641-1849

Marine Midland Bank
UNITED STATES OF AMERICA
Corporate Headquarters
One Marine Midland Center
Buffalo, NY 14203
Telephone: (716) 841-2424
Facsimile: (716) 841-5391

Midland Bank plc
UNITED KINGDOM
Head Office
27-32 Poultry
London EC2P 2BX
Telephone: 0171-260 8000
Facsimile: 0171-260 7065

The Saudi British Bank
SAUDI ARABIA
Head Office
Al Amir Adbul Aziz Ibn Mossaad Ibn Jalawi Street, Riyadh
Telephone: (01) 405-0677
Facsimile: (01) 405-0660

UBAF Bank Limited
UNITED KINGDOM
30 Gresham Street
London EC2V 7LP
Telephone: 0171-606 7777
Facsimile: 0171-600 3318

INVESTMENT BANKING

HSBC Investment Bank Limited
UNITED KINGDOM
Thames Exchange, 10 Queen Street Place
London EC4R 1BL
Telephone: 0171-621 0011
Facsimile: 0171-621 0496

INVESTMENT BANKING — MERCHANT BANKING

Equator Bank Limited
BAHAMAS
Suite 102, Saffrey Square
Bank Lane and Bay Street, Nassau
Telephone: (809) 322-2754
Facsimile: (809) 326-5706

HSBC Capital Limited
HSBC Corporate Finance Limited
HSBC Investment Bank Asia Holdings Limited
HONG KONG
7/F, Hutchison House
10 Harcourt Road
Telephone: 2841 8888
Facsimile: 2845 9047

Montagu Private Equity Limited
Samuel Montagu & Co. Limited
UNITED KINGDOM
10 Lower Thames Street
London EC3R 6AE
Telephone: 0171-260 9000
Facsimile: 0171-488 1630

INVESTMENT BANKING — EQUITY SECURITIES

James Capel & Co. Limited
UNITED KINGDOM
Thames Exchange
10 Queen Street Place
London EC4R 1BL
Telephone: 0171-621 0011
Facsimile: 0171-621 0496

James Capel Asia Limited
HONG KONG
5/F, Hutchison House
10 Harcourt Road
Telephone: 2843 9111
Facsimile: 2810 7673

James Capel Incorporated
UNITED STATES OF AMERICA
250 Park Avenue
New York, NY 10177
Telephone: (212) 808-0500
Facsimile: (212) 687-1650

Kay Hian James Capel Pte. Ltd.
SINGAPORE
80 Raffles Place
#30-01 UOB Plaza 1
Singapore 0104
Telephone: 533 2936
Facsimile: 532 6919

Wardley Financial Services Limited
HONG KONG
3/F, Hutchison House
10 Harcourt Road
Telephone: 2521 1661
Facsimile: 2810 0145

INVESTMENT BANKING — PRIVATE BANKING AND TRUSTEE

The British Bank of the Middle East
SWITZERLAND
Quai General Guisan 2, 1204 Geneva
Telephone: (22) 311 9611
Facsimile: (22) 781 0384

Guyerzeller Bank AG
SWITZERLAND
Genferstrasse 6-8, CH-8027 Zurich
Telephone: (1) 206 7111
Facsimile: (1) 206 7397

HSBC International Trustee Limited
HSBC Private Bank (Jersey) Limited
HSBC Trustee (Jersey) Limited
Midland Bank Trustee (Jersey) Limited
CHANNEL ISLANDS
1 Grenville Street, St Helier
Jersey JE2 4UF
Telephone: 01534-606500
Facsimile: 01534-606504

Principal Offices *(continued)*

HSBC Investment Bank Asia Limited
HONG KONG
6/F, Hutchison House
10 Harcourt Road
Telephone: 2841 8888
Facsimile: 2845 9047

HSBC Trustee (Hong Kong) Limited
HONG KONG
Level 13, 1 Queen's Road Central
Telephone: 2533 6333
Facsimile: 2810 5259

Midland Bank Trust Company Limited
UNITED KINGDOM
2/F, Norwich House, Nelson Gate
Commercial Road
Southampton SO15 1GX
Telephone: 01703-723 722
Facsimile: 01703-723 587

Trinkaus & Burkhardt KGaA
GERMANY
Konigsallee 21/23
D-40212 Dusseldorf 1
Telephone: (211) 910 0
Facsimile: (211) 910 2691

INVESTMENT BANKING — ASSET MANAGEMENT

HSBC Asset Management Americas Inc.
UNITED STATES OF AMERICA
3rd Floor, 250 Park Avenue, New York
NY 10177-0012
Telephone: (212) 503 6815
Facsimile: (212) 503 6620

HSBC Asset Management Europe Limited
HSBC Unit Trust Management Limited
UNITED KINGDOM
6 Bevis Marks
London EC3A 7QP
Telephone: 0171-955 5050
Facsimile: 0171-955 5052

HSBC Asset Management Hong Kong Limited
HONG KONG
10/F Citibank Tower
3 Garden Road
Telephone: 2801 0111
Facsimile: 2845 0226

CAPITAL MARKETS

HSBC Greenwell
UNITED KINGDOM
Thames Exchange
10 Queen Street Place
London EC4R 1BQ
Telephone: 0171-336 3000
Facsimile: 0171-220 7113

HSBC Securities, Inc.
UNITED STATES OF AMERICA
140 Broadway, New York, NY 10005
Telephone: (212) 825 6780
Facsimile: (212) 825 3861

FINANCE

Forward Trust Group Limited
UNITED KINGDOM
145 City Road, London EC1V 1JY
Telephone: 0171-251 9090
Facsimile: 0171-490 0993

HSBC Finance (Malaysia) Berhad
MALAYSIA
3/F, Plaza See Hoy Chan
Jalan Raja Chulan
50200 Kuala Lumpur
Telephone: (03) 2325255
Facsimile: (03) 2306514

HSBC International Trade Finance Limited
UNITED KINGDOM
1/F, St Magnus House
3 Lower Thames Street
London EC3R 6HA
Telephone: 0171-260 5937
Facsimile: 0171-260 4829

MidAval Asia Pte Ltd
SINGAPORE
21 Collyer Quay
#19-03 HongkongBank Building
Singapore 0104
Telephone: 2242477
Facsimile: 2258021

Mortgage And Finance Berhad
BRUNEI DARUSSALAM
Shops No. 3 and 4
Goodwood Building
Mile 2 Jalan Gadong
Bandar Seri Begawan 3180
Telephone: (02) 427969, 427970
Facsimile: (02) 448474

Wayfoong Credit Limited
Wayfoong Finance Limited
HONG KONG
18/F, Leighton Centre
77 Leighton Road
Telephone: 2839 6333
Facsimile: 2895 4845

Wayfoong Mortgage And Finance (Singapore) Limited
SINGAPORE
6 Claymore Hill
#03-01 Claymore Plaza
Singapore 0922
Telephone: 7377977
Facsimile: 7378997

INSURANCE, RETIREMENT BENEFITS, ACTUARIAL AND PERSONAL FINANCIAL SERVICES

Carlingford Insurance Company Limited
HONG KONG
40/F, Sun Hung Kai Centre
30 Harbour Road, Wanchai
Telephone: 2827 3322
Facsimile: 2827 7636

Gibbs Hartley Cooper Limited
UNITED KINGDOM
Bishops Court
27/33 Artillery Lane
London E1 7LP
Telephone: 0171-247 5433
Facsimile: 0171-377 2139

Hexagon Insurance Services Limited
UNITED KINGDOM
Hexagon House
Cletta Park
Newport, Gwent NP1 9XT
Telephone: 01633-654300
Facsimile: 01633-817910

HSBC Insurance Holdings Limited
UNITED KINGDOM
Bishops Court
27/33 Artillery Lane
London E1 7LP
Telephone: 0171-247 5433
Facsimile: 0171-247 7373

HSBC Life Limited
HONG KONG
Suite 602, Citicorp Centre
18 Whitfield Road
Telephone: 2802 6388
Facsimile: 2806 1892

Midland Life Limited
UNITED KINGDOM
Norwich House
Nelson Gate
Commercial Road
Southampton SO15 1GX
Telephone: 01703-229929
Facsimile: 0117-251993

BULLION DEALING AND COMMODITY/BROKERAGE SERVICES

Wardley Broking Services Private Limited
SINGAPORE
21 Collyer Quay
#17-01 HongkongBank Building
Singapore 0104
Telephone: 2254007
Facsimile: 2249201

PROPERTY

Wayfoong Property Limited
HONG KONG
31/F, Hopewell Centre
183 Queen's Road East
Telephone: 2822 7211
Facsimile: 2861 2492

SHIPPING SERVICES

HSBC Shipbrokers Limited
HONG KONG
4/F, Hutchison House
10 Harcourt Road
Telephone: 2841 8580
Facsimile: 2810 0885

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Central Registration Hong Kong Limited
19th Floor, Hopewell Centre
183 Queen's Road East, Hong Kong

本年報備有中譯本，如欲查閱可向下列公司索取：
香港皇后大道東一八三號合和中心十九樓
香港中央證券登記有限公司

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HSBC Holdings plc
10 Lower Thames Street, London EC3R 6AE, United Kingdom