The Hongkong and Shanghai Banking Corporation Limited

(Incorporated in Hong Kong SAR with limited liability)

Basel III – Pillar 3 disclosures of India Branches

For the period ended 31 December 2013

1 Scope of Application

The capital adequacy framework applies to The Hongkong and Shanghai Banking Corporation Limited – India Branches ("the Bank"). The Bank has a subsidiary, HSBC Agency (India) Private Limited, which is consolidated in line with AS 21 and full capital deduction is taken for stand-alone financials. The Bank does not have any other Group company where a pro-rata consolidation is done or any deduction is taken. The Bank holds minority interests (2.07% shareholding) in a Group entity HSBC Professional Services (India) Private Limited which is neither consolidated nor is capital deducted. The investment in this company is appropriately risk weighted.

(i) Capital deficiencies in all subsidiaries not included in the consolidation

The aggregate amount of capital in HSBC Agency (India) Private Limited of Rs. 0.2M is not included in the consolidation and is deducted from capital.

(ii) Bank's total interest in insurance entities

The Bank has no interest in any of the insurance entities of the Group.

2 Capital Structure

(i) Composition of Tier 1 capital

(Rs '000)

	As at 31 December 2013
Capital	44,991,660
Reserves	91,387,512
Less: Deductions from Tier I Capital	**(7,106,778)**
- Intangible Assets (Deferred Tax Asset)	(5,865,851)
- Investment in subsidiaries in India	(200)
- Debit Value Adjustments (DVA) (note 1)	(1,143,311)
- Defined Benefit Pension Fund Asset	(97,416)
Total Tier I Capital	**129,272,394**

Note 1: In line with the Master Circular – Basel-III Capital Regulations dated 1 July 2013 the Bank has deducted DVA from Tier 1 capital (Refer para 5.6 (aa) of the financial statements).

(ii) Tier 2 capital

(Rs '000)

	As at 31 December 2013
Property revaluation reserves	3,648,218
General Loss Reserves and Investment Reserves	8,369,669
Total Tier II Capital	**12,017,887**

2 Capital Structure *(Continued)*

(iii) Debt capital instruments in Tier 2 capital

No debt capital instruments are included in Tier 2 capital.

(iv) Subordinated debt in Tier 2 capital

There is no amount outstanding in respect of subordinated debt as at 31 December 2013.

(v) Other deductions from capital

There are no other deductions from capital.

(vi) Total eligible capital

The total eligible capital is Rs. 141,290M.

3 Capital Adequacy

The Bank's capital management framework is shaped by its structure, business model and strategic direction. There is a continuing need to focus on effective management of risk and commensurate capital to bear that risk. The Bank carefully assesses its growth opportunities relative to the capital available to support them, particularly in light of the economic environment and advent of Basel III. The Basel III capital rules became effective from 1 April 2013 except for those relating to Credit Valuation Adjustment (CVA) risk capital charge for over the counter derivatives. As per the circular issued by RBI on December 31, 2013, these rules would become effective from 1 April 2014.

We continue to monitor developments and believe that our current robust capital adequacy position means we are well placed for continuing compliance with the Basel III framework.

The Bank maintains a strong discipline over capital allocation and ensuring that returns on investment cover capital costs.

(i) Capital requirements for Credit Risk, Market Risk and Operational Risk

(Rs '000)

	As at 31 December 2013
I. Capital required for Credit Risk	**53,114,600**
- For portfolios subject to Standardised approach	53,114,600
II. Capital required for Market Risk (Standard Duration Approach)	**12,599,291**
- Interest rate risk	11,804,040
- Foreign exchange risk	720,000
- Equity risk	75,251
- Securitisation exposure	-
III. Capital required for Operational Risk (Basic Indicator Approach)	**8,402,010**
Total capital requirement (I + II + III)	74,115,901
Total capital funds of the Bank	141,290,280
Total risk weighted assets	823,510,009
Common Equity Tier I Capital (CET1)	15.70%
Tier I capital ratio	15.70%
Tier II capital ratio	1.46%
Total capital ratio	17.16%

There is no significant subsidiary for which the above disclosure is required.

4 Credit risk:

a. General

Credit Risk is the risk of financial loss if a customer or counterparty fails to meet an obligation under a contract. It arises principally from direct lending, trade finance, marked-to-market exposure from derivative contracts and certain off-balance sheet products such as guarantees and from the Bank's holdings of assets in the form of debt securities.

Strategy and Processes

The HSBC Group Head Office formulates high-level risk management policies for the HSBC Group worldwide. The Bank has formulated local credit guidelines consistent with HSBC policy and Reserve Bank of India's (RBI) guidelines. The Bank's risk management policies and procedures are subject to a high degree of oversight and guidance to ensure that all types of risk are systematically identified, measured, analysed and actively managed.

The Bank has standards, policies and procedures dedicated to the monitoring and management of credit risk, which include the following:

- Establish a separate Risk Management unit independent of business with a matrix of delegated approval authorities for the approval of credit risks.
- Establish and maintain the exposure norms policy. This policy delineates the Bank's maximum exposures to individual customers, customer groups and other risk concentrations. This policy also ensures compliance with the ceilings and lending guidelines relating to specific market sectors and industries.
- Establish and monitor the credit appetite for particular sectors and the minimum criteria that must be met by new customers.
- Constitute a Risk Management Committee ("RMC") consisting of senior executives, which reviews overall portfolio risks and key risks facing the Bank in India.
- Undertake independent review and objective assessment of the credit risk. All commercial non-bank credit facilities originated are subject to review prior to the facilities being committed to customers.
- Control exposures to banks and other financial institutions. The Group's credit and settlement risk limits to counterparties in the finance and government sectors are designed to optimise the use of credit availability and avoid excessive risk concentration.
- Manage exposures to debt securities by establishing controls in respect of the liquidity of securities held for trading and setting issuer limits for financial investments. Separate portfolio limits are established for asset-backed securities and similar instruments.
- Control cross-border exposures to manage country and cross-border risk through the imposition of country limits with sub-limits by maturity and type of business.

4 Credit risk: *(Continued)*

a. General *(Continued)*

Strategy and Processes ***(Continued)***

- Maintain and develop HSBC's risk rating framework and systems in order to classify exposures meaningfully and facilitate focused management of the risks involved. Rating methodologies are based upon a wide range of financial analytics together with market data-based tools, which are core inputs to the assessment of customer risk. For larger facilities, while full use is made of automated risk rating processes, the ultimate responsibility for setting risk ratings rests with the final approving executive. Risk grades are reviewed frequently and amendments, where necessary, are implemented promptly.

Structure and Organisation

Credit approval authorities are delegated from the Chief Risk Officer at the Regional Head Office in Hong Kong to the Chief Executive Officer, India and the Chief Risk Officer, India. The Chief Risk Officer in India maintains a strong functional reporting line to the Chief Risk Officer in Hong Kong.

The Risk Management function is responsible for the quality and performance of its credit portfolios and for monitoring and controlling all credit risks in its portfolios, including those subject to approval by the Regional Head Office in Hong Kong.

Scope and nature of risk reporting, measurement, monitoring and mitigation

The Bank manages and directs credit risk management systems initiatives. HSBC has constructed a centralized database covering substantially all of the Group's direct lending exposures, to deliver an increasingly granular level of management reporting.

The Bank is required to maintain regular reporting on its credit risk portfolio, to include information on large credit exposures, concentrations, industry exposures, levels of impairment provisioning and country exposures.

Non performing advances

Non performing advances are identified by periodic appraisals of the portfolio by management or in accordance with RBI guidelines, whichever is earlier.

Specific provisions are made on a case-by-case basis based on management's assessment of the degree of impairment of the advances (other than homogeneous unsecured retail loans), subject to the minimum provisioning levels prescribed by the RBI. When there is no longer any realistic prospect of recovery, the outstanding advance is written off.

4 Credit risk: *(Continued)*

a. General *(Continued)*

Non performing advances *(Continued)*

Special attention is paid to problem exposures, which are subject to more frequent and intensive review and reporting, in order to accelerate remedial action. The bank engages with customers closely to work out of distress situations.

Subject to the minimum provisioning levels prescribed by the RBI, the provision on homogeneous unsecured loans relating to retail business is assessed on a portfolio basis using the historical loss and/or net flow rate method.

b. Disclosures for portfolios under the standardised approach

The Bank uses the following External Credit Assessment Institutions (ECAIs) approved by RBI to calculate its capital adequacy requirements under the standardised approach to credit risk for Corporate, Bank and Sovereign counterparties.

Domestic ECAIs for external ratings of Indian Corporates:

a) Credit Analysis and Research Limited;

b) CRISIL Limited;

c) India Ratings and Research Private Limited;

d) ICRA Limited; and

e) Brickwork Ratings India Private Limited.

The Bank used the ratings issued by the ECAIs (for both long term and short term facilities) to risk weight both funded as well as non-funded exposures to corporate customers.

The process used by the Bank to transfer public issue ratings onto comparable assets in the banking book is in line with the provisions advised in RBI's Prudential Guidelines on Capital Adequacy and Market Discipline issued on 2 July 2012.

The mapping of external credit ratings and risk weights for corporate exposures is provided in the grids below:

Risk weight mapping of long term corporate ratings

Long term ratings	Risk weights
AAA	20%
AA	30%
A	50%
BBB	100%
BB & Below	150%
Unrated	100%

4 Credit risk: *(Continued)*

b. Disclosures for portfolios under the standardised approach *(Continued)*

Risk weight mapping of short term corporate ratings

	Short Term Ratings			Risk weights
CARE	**CRISIL**	**FITCH**	**ICRA**	
CARE A1	CRISIL A1	FITCH A1	ICRA A1	30%
CARE A2	CRISIL A2	FITCH A2	ICRA A2	50%
CARE A3	CRISIL A3	FITCH A3	ICRA A3	100%
CARE A4	CRISIL A4	FITCH A4	ICRA A4	150%
CARE D	CRISIL D	FITCH D	ICRA D	150%
Unrated	Unrated	Unrated	Unrated	100%

The claims on banks incorporated in India and foreign banks branches in India, excluding investment in equity shares and other instruments eligible for capital status, are risk weighted as shown below:

Capital to Risk weighted Assets Ratio %	Scheduled Banks	Other Banks
> 9	20%	100%
6 to < 9	50%	150%
3 to < 6	100%	250%
0 < 3	150%	350%
Negative	625%	625%

International ECAIs for external ratings of Foreign Banks, Foreign Sovereigns, Foreign Public Sector Entities and Non-Resident Corporates:

a) Fitch;

b) Moodys; and

c) Standard & Poor's (S & P)

The process used by the Bank to transfer public issue ratings onto comparable assets in the banking book is in line with the provisions advised in RBI Guidelines.

The mapping of external credit ratings and risk weights for the above entities are provided in the grids below:

Risk weight mapping of foreign banks

S&P and Fitch ratings	AAA to AA	A	BBB	BB to B	Below B	Unrated
Moody's rating	Aaa to Aa	A	Baa	Ba to B	Below B	Unrated
Risk weight	20%	50%	50%	100%	150%	50%

4 Credit risk: *(Continued)*

b. Disclosures for portfolios under the standardised approach *(Continued)*

Risk weight mapping of foreign sovereigns

S&P and Fitch ratings	AAA to AA	A	BBB	BB to B	Below B	Unrated
Moody's rating	Aaa to Aa	A	Baa	Ba to B	Below B	Unrated
Risk weight	0%	20%	50%	100%	150%	100%

Risk weight mapping of foreign public sector entities

S&P and Fitch ratings	AAA to AA	A	BBB	Below BB	Unrated
Moody's rating	Aaa to Aa	A	Baa to Ba	Below Ba	Unrated
Risk weight	20%	50%	100%	150%	100%

Risk weight mapping of non resident corporates

S&P and Fitch ratings	AAA to AA	A	BBB	Below BB	Unrated
Moody's rating	Aaa to Aa	A	Baa to Ba	Below Ba	Unrated
Risk weight	20%	50%	100%	150%	100%

Policy for Collateral Valuation and Management

It is the Bank's policy that all corporate and institutional facilities be reviewed (and hence revalued) at least on an annual basis. All deeds of ownership/titles related to collateral are held in physical custody under control of executives independent of the business.

For mortgages, the credit policy clearly outlines the acceptable Loan to value ratio (LVR) for different types of properties. The maximum LVR offered to customers was capped at 80% of the mortgaged property since 1 April 2011, except if approved under a special lending authority.

The valuation of property is initiated through a bank-empanelled valuer who is an expert on the subject matter. Additionally, for loans exceeding INR 5 million, dual valuations are also initiated in order to have the benefit of a second opinion on the mortgaged property. The disbursal of the loan is handled through an empanelled lawyer who in exchange collects the security documents from the borrower. The property documents thus collected are attached to the credit file and sent to central archives where the same is stored in a secure manner.

INM has developed an in-house Property Price Index (PPI) which is used to measure the actual LVR of the properties financed by the Bank. The methodology for PPI development has been approved by Risk and refreshed every 6 months. However, should a loan become a non-performing asset (NPA), a fresh valuation is initiated through the bank-empanelled valuer and the provisions applicable are calculated accordingly.

4 Credit risk: *(Continued)*

b. Disclosures for portfolios under the standardised approach *(Continued)*

Main Types of Collateral taken by HSBC

The main types of recognised collateral taken by the Bank appear in the list of eligible financial collaterals advised in Section 7.3.5 of RBI's Prudential Guidelines on Capital Adequacy and Market Discipline, and include (but are not limited to) cash on deposits, equities listed in a main index and/or a recognised exchange, units or shares in collective investment schemes and various recognised debt securities. Further the main types of recognised collateral taken by the Bank for mortgages include plots of land, ready possession and under construction properties.

Main Types of Guarantor Counterparty and their Creditworthiness

As stated in Section 7.5 of the RBI's Prudential Guidelines on Capital Adequacy and Market Discipline, certain guarantees are recognised for credit risk mitigation purposes. The main types of guarantees are from sovereigns, corporates and banks. For a corporate guarantee to be recognised as a credit risk mitigant for the purposes of capital adequacy calculation, the guarantee provider must have a credit rating equivalent to AA- or better from a rating agency recognised by the RBI.

Information about (Market or Credit) Risk Concentrations within the mitigation taken

The quantum of the credit portfolio which benefits from financial collaterals and/or guarantees as credit risk mitigants is an insignificant portion of the customer advances of the Bank. Therefore the credit and/or market concentration risks are not material

The total exposure (including non-funded post credit conversion factors) that is covered by eligible financial collateral, after the application of haircuts is Rs. 69,178M.

(i) Total gross credit risk exposures by geography

(Rs '000)

	Fund based [Note 1]	Non fund based [Note 2]	As at 31 December 2013 Total
Overseas	-	-	-
Domestic	522,778,005	632,221,981	1,154,999,986
Total	**522,778,005**	**632,221,981**	**1,154,999,986**

Note 1: Amount represents funded exposure before credit risk mitigants.

Note 2: Amount represents non-funded exposure after applying credit conversion factor and before credit risk mitigants.

4 Credit risk: *(Continued)*

b. Disclosures for portfolios under the standardised approach *(Continued)*

(ii) Industry type distribution of exposures as at 31 December 2013

(Rs '000)

Industry	Fund based	Non Fund based	Total
Mining and Quarrying	465,454	737,608	1,203,062
Food Processing	7,102,883	2,269,663	9,372,546
Beverages and Tobacco	1,193,882	2,103,458	3,297,340
Textiles	4,753,840	5,013,082	9,766,922
Leather and Leather products	167,171	263	167,434
Wood and Wood Products	-	19,923	19,923
Paper and Paper Products	6,459,821	2,433,885	8,893,706
Petroleum	86,681	31,629,306	31,715,987
Chemicals and Chemical Products	39,930,517	38,396,021	78,326,538
Rubber, Plastic and their Products	4,675,162	1,471,847	6,147,009
Glass & Glassware	3,109,002	1,656,891	4,765,893
Cement and Cement Products	4,526,324	3,340,148	7,866,472
Basic Metal and Metal Products	13,242,924	26,002,015	39,244,939
All Engineering	17,539,913	41,686,864	59,226,777
Vehicles and Transport Equipments	15,857,316	13,397,741	29,255,057
Gems and Jewellery	381,573	-	381,573
Construction	24,911,627	2,964,677	27,876,304
Infrastructure	16,696,162	44,093,270	60,789,432
NBFCs and trading	24,006,672	7,607,895	31,614,567
Banking and finance	700,000	221,878,223	222,578,223
Computer Software	377,747	2,555,902	2,933,649
Other Industries	255,745,672	174,631,627	430,377,299
Retail	80,847,662	8,331,672	89,179,334
Total	**522,778,005**	**632,221,981**	**1,154,999,986**

4 Credit risk: *(Continued)*

b. Disclosures for portfolios under the standardised approach *(Continued)*

(iii) Residual contractual maturity breakdown of total assets

(Rs '000)

	As at 31 December 2013
1 day	175,061,847
2 to 7 days	15,812,395
8 to 14 days	21,535,019
15 to 28 days	70,847,531
29 days & up to 3 months	154,776,855
Over 3 months and up to 6 months	132,113,501
Over 6 months and up to 1 year	144,044,171
Over 1 year and up to 3 years	202,634,255
Over 3 years and up to 5 years	107,629,498
Over 5 years	176,160,338
Total	**1,200,615,410**

(iv) Amount of Non-Performing Assets (NPAs) (Gross)

(Rs '000)

	As at 31 December 2013
Substandard	1,889,948
Doubtful 1	2,270,894
Doubtful 2	921,703
Doubtful 3	1,442,658
Loss	742,809
Total	**7,268,011**

(v) Net NPA

The net NPA is Rs 1,656M. Please see table (vii) below

(vi) NPA ratios

	As at 31 December 2013
Gross NPAs to gross advances	2.12%
Net NPAs to net advances	0.49%

4 Credit risk: *(Continued)*

b. Disclosures for portfolios under the standardised approach *(Continued)*

(vii) Movement of NPAs

(Rs '000)

	As at 31 December 2013		
	Gross NPA's	**Provision**	**Net NPA**
Opening balance as at 1 April 2013	6,408,323	5,218,253	1,190,170
Additions during the period	2,535,300	937,696	1,597,604
Reductions during the period	(1,675,612)	(544,281)	(1,131,331)
Closing balance as at 31 December 2013	**7,268,011**	**5,611,567**	**1,656,444**

(viii) Non performing investments

Non performing investments as at 31 December 2013 are Rs. 6.

This represents 3 equity share investments (previous year Rs.3) and 3 preference share investments (previous year Rs.2) which have each been written down to Rs. 1.

(ix) Movement of provisions for depreciation on investments

(Rs '000)

	As at 31 December 2013
Opening balance	1,097,728
Provisions during the year	301,091
Write offs during the year	-
Write back of excess provisions during the year	-
MTM on hedging swaps reclassified as trading swaps as at 31 December 2013	-
Closing balance	**1,398,819**

(x) Exposure under various risk buckets (post Credit Risk Mitigants)

(Rs '000)

	As at 31 December 2013
Below 100% risk weight	890,332,383
100% risk weight	348,272,678
Above 100% risk weight	27,299,197
Deductions*	(7,106,778)
Total	**1,258,797,480**

* Deduction represents amounts deducted from Capital Funds