HSBC

Transcript

Investor & Analyst Call
Annual Results

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NOEL QUINN, GROUP CHIEF EXECUTIVE: Good morning to everyone in the room in London today. Great to see you all again. And good afternoon to those watching from Hong Kong and around the world. Before Georges takes you through the Q4 numbers, I'll start with a summary of our strategic progress.

When we started our transformation three years ago, we also revisited our core purpose and values. Opening up a world of opportunity is the reason HSBC exists. We are making it a reality for our customers. Our results today are evidence of that, and I'm pleased that our performance also demonstrates that our people are living and breathing our values, particularly the fourth value, which is 'get it done'. I will demonstrate during the discussion today that we have achieved a lot over the last three years and that we are committed to doing even more.

I want to start by telling you the three elements I'm going to cover in the presentation today. Transformation was the first phase of our strategy execution. Three years ago, fair criticism of HSBC was that unprofitable or subscale businesses and clients were dragging down good profitability from our international proposition and from the profits generated in Hong Kong and the UK. I'm pleased to say we've addressed this. Our international connectivity is now underpinned by good, broad-based profit generation around the world.

Delivery in 2022 is all about the good set of results we've just announced. I will come to the detail later, but I'm pleased adjusted profits before tax were up 17%. We're firmly on track to achieve our returns target for 2023 onwards, and we expect to have substantial distribution capacity for higher dividends, more buybacks and, potentially, a special dividend in early 2024.

But there's also so much more we can achieve. So the final element of the presentation is growth and returns. It's all about how we will further improve performance going forward. As we've transformed, we've built a strong platform for the future that will enable us to meet our customers' needs, and I expect wealth, payments and FX, fee income, technology investment and climate finance to provide new value creation opportunities in the years to come.

So taking these three messages in turn, starting with transformation, three years ago we set out to tackle a series of fundamental problems – loss-making businesses, unprofitable products and clients, inefficient capital, and costs. Our transformation journey had six components, which I will run through in more detail on the following slides.

Our international connectivity remains our biggest differentiator, and we've grown and protected many of our market-leading international businesses during the three years, but we've done that while repositioning unprofitable and non-strategic businesses, particularly in the US and Europe. That's resulted in a client proposition that is now built on international connectivity underpinned by our broad base of geographic profit penetration.

All of this has been supported by strong cost discipline, which has enabled us to drive a step change in our technology investment. We've also removed the dilutive scrip dividend and introduced a new sustainable dividend policy, which is delivering attractive ongoing returns for shareholders and enabling us to invest in the business. Crucially, we've created a strong platform for improved growth and returns, with new opportunities for value creation. Our focus now is to capitalise on these opportunities.

Taking each of these in turn, in terms of international connectivity, our greatest strength remains our ability to connect the world's major trading and investment blocs. We are the world's number one trade bank, top three for FX, and a leading payments company. Last year, we processed more than $600 trillion of payments globally. International is also core to our value proposition. Around 45% of our wholesale client business is done cross-border. In Wealth and Personal Banking, we now have six million international customers, which is up 7% on last year. This is significant, because our international customers generate around twice the average revenue as our domestic customers.

Our international connectivity has also translated into higher revenue and market share. Since 2019, we've grown Global Payment Solutions revenue by 6% CAGR, Trade revenue by 5% CAGR, and revenue from Global Foreign Exchange has increased by 12% CAGR. Overall, Transaction Banking revenue was up by 7% CAGR over the last three years.

We also see an opportunity to create even more value by continuing to grow these product lines over the coming years. The next slide drills down into how we reshaped our portfolio. Across the group, we reduced risk-weighted assets by a cumulative $128 billion, well in excess of our target of $110 billion. We made key strategic decisions to sell our US mass-market retail bank, our retail banking operations in France, and our banking business in Canada. We've also announced exits from Russia and Greece, with other potential smaller exits being considered. We've reallocated more of our capital to Asia – and by Asia, I mean the whole of Asia. We want to build strong wealth businesses in mainland China, India and Singapore, alongside strong business we already have in Hong Kong.

We accelerated this process through bolt-on acquisitions and investments in the last 12 months. We've completed the integration of AXA Singapore and L&T Investment Management in India. And in mainland China, as well as continuing the organic buildout of Pinnacle, we had seven main licence approvals since 2020. These enabled us to take full ownership of HSBC Life China and increase our majority stake in HSBC Shanghai to 90%.

As I said earlier, we now have an international connectivity underpinned by good, broad-based profit generation, as this slide demonstrates. This is the single biggest change compared to three years ago. I won't go through all the numbers on this slide, but I will mention a few. The total amount of adjusted profit contributed by Asia excluding Hong Kong and mainland China was more than $4 billion in 2022 – an increase of 23% compared to 2019. Mainland China excluding associate income from BoCom contributed around $1 billion of profit last year in a challenging year, and India contributed a further $900 million of adjusted profit.

Outside Asia, the Middle East generated $1.8 billion of adjusted profits last year. HSBC UK delivered $5 billion of adjusted profits. And we've got leaner, more profitable businesses in continental Europe and the US. Continental Europe generated adjusted profits of over $2 billion, and the US adjusted profits of over $1 billion. Both of those businesses were close to loss-making, or loss-making, three years ago.

Mexico is another high-returning business. It delivered a return on tangible equality of 18%, and worthy of note is that 60% of new-to-bank retail customers last year were acquired through corporate client relationships by the provision of employee banking services and payroll services, demonstrating the value of our connected model in the country.

The next slide focuses on the tight cost discipline we've demonstrated and we will maintain. The reduction of our global corporate real estate, our branch network and operations headcount have all delivered material savings, and we expect to achieve further efficiencies in the years to come, but the most important point on this slide is that we've used these cost savings to increase investment in technology. 18% out in operations costs, 18% in in technology investment. This is spending in the right place to build the business of the future, and it has enabled us to fundamentally change the way we operate.

Our formal three-year cost reduction programme has now ended, but we still expect more than $1 billion of cost saves to flow through into 2023 from that programme. There will be no easing up at all in our cost discipline, but I think it's right that we will also continue to identify opportunities to create efficiencies going forward that will deliver sustainable cost savings in future years, with any associated costs from those programmes reported through the cost line, not treated below the line as significant items.

Whilst we have transformed, we have also invested in areas that we expect to deliver strong growth and returns in the future. A strong balance sheet has always been a defining characteristic of HSBC, and we've continued to grow the deposit book and assets over the past three years. This is benefiting our performance now that rates have increased.

Developing our Wealth business has also been a strategic priority. Our investments over the past three years are gaining traction, reflected in revenues of over $9 billion in 2022, excluding market impacts, which is a 9% CAGR compared to 2020. It's also reflected by increased insurance market share in Hong Kong.

The next slide sets out the impact of the step change we made in technology investment. The faster services, reduced friction and more competitive products that this investment has enabled has been critical to improving the customer experience. With our digital propositions, our aim is to build once, deploy globally. Our upgraded mobile banking app is available in 24 markets and has around 13 million active customers. HSBC Kinetic, our award-winning business banking app in the UK, now has around 53,000 new-to-bank customers. And as well as Global Wallet and Global Money, we have rolled out our new digital trade finance platform in Hong Kong and the UK, so that our market-leading businesses are well positioned for the next 10 years. In addition, we are launching new products like HSBC Orion, which is our proprietary tokenisation bond issuance platform using blockchain. The first public bond was priced on it last month.

Turning now to delivery in 2022, I'm pleased with our '22 performance. As you know from Q3, the reported numbers include a $2.4 billion impairment for the planned disposal of our French retail business. Adjusted revenue was up 18% on the back of a strong net interest income performance, and adjusted profits were up 17%. We delivered a good cost outcome in a high inflation environment by containing adjusted cost growth to around 1%. Expected credit losses were a $3.6 billion charge. The dividend was 32 cents per share. The CET1 ratio was 14.2%. And we achieved a reported RoTE of 9.9%, or 11.6% once you strip out significant items, so we're firmly on track to deliver returns of 12% plus from 2023 onwards.

I'm now going to quickly run through our four strategic pillars, starting with 'Focus on our strengths'. Our market-leading Commercial Banking franchise had a very good year. Adjusted revenue was up almost 30% on last year. There was further good growth in Trade, and Global Payment Solutions benefited from higher interest rates. It was encouraging to see fee income grow by 8%, and there was strong adjusted revenue growth across all regions.

In Wealth and Personal Banking, revenue was up 16% overall. Personal Banking had a particularly strong year, and lending balances were up 3%, despite subdued economic conditions in Hong Kong. Wealth was also up, excluding market impacts. One of the best signs that our Wealth strategy is gaining traction is net new invested assets of $80 billion in 2022 – an increase of 25% compared to 2021. This is highly promising for future revenue generation. There was also continued growth in the value of new business in our Asia insurance franchise, despite adverse market conditions. Again, there was strong revenue growth in all geographies.

Global Banking and Markets also performed very well in 2022. Markets and Securities Services was up 14%, due mainly to rate rises and a standout Foreign Exchange performance. Banking was up 17%, also mainly due to higher rates. In a challenging year for investment banking globally, this good performance underlines the resilience of our model. Collaboration revenues from cross-selling Global Banking and Markets products to customers in Commercial Banking and Wealth and Personal Banking were up 6%. There was strong growth in client business booked in the east but originated in Europe and the Americas, up around 30% on the previous year. This again underlines geographic diversification of our revenues, and that our greatest strength is connecting the world's major economic blocs.

The next slide is on 'Digitise at scale', our second pillar. It illustrates the outcomes of our increasing investment in technology. Within retail and wholesale, penetration levels increased materially. More than 75% of Commercial Banking customers are now digitally active, and almost half of retail customers are now mobile active. We also believe we can grow these numbers further.

The next slide covers 'Energise for growth' and how we're changing the culture of HSBC. Taking out unnecessary layers of management has helped increase our speed and agility. In our last staff survey, the number of colleagues who say that work processes allow them to work efficiently were six percentage points above the sector benchmark. Confidence within the organisation has also increased. 77% of our colleagues told us that they are confident about our future which is seven percentage points above the sector benchmark and an increase of three percentage points since 2021. We made further progress against our diversity commitments, with increases in representation of female leaders and black heritage leaders. 36% of our key leadership roles are now located in Asia, and, if I reflect on the leadership of our Asian business five years ago versus today, I see much more Asian heritage talent and a strong pipeline of talent coming through that we continue to develop. At the same time, we know we have more to do in all these areas.

The next slide looks at our final pillar and the leading role that we play in the 'Transition to net zero'. The amount of sustainable financing and investment provided and facilitated in 2022 was up slightly despite the market for green, social, sustainable and sustainability-linked bonds being substantially down. The cumulative total amount since the start of 2020 is now $211 billion. We've set new targets for on balance sheet-financed emissions for six high-emitting sectors. We recognise that methodologies and data for measuring emissions will continue to evolve, and our own disclosures will therefore continue to evolve as well. We continue to reduce emissions across our own operations and supply chain, which were down more than 58% since 2019.

Finally, my third message is about growth and returns. We are firmly on track to deliver returns of at least 12% in 2023, but there's also so much more we can achieve, and we can deliver higher growth and returns as we move out of transformation and into value creation. We plan to grow our core businesses, which are built on our international connectivity and the strong broad-based growth we have now spanning every region. The investment we've made in new sources of value creation, wealth, payments and FX, fee income, technology and sustainability will all increase and diversify our revenue, and we won't be relinquishing our grip on costs because it enables us to spend in areas that create value.

Our improved profitability and sustainable dividend policy will give us a substantial distribution capacity, with a 50% dividend pay-out ratio established for 2023 and 2024, a return to quarterly dividends from Q1, the consideration of buybacks brought forward to the Q1 results and, on top of this, the consideration of a special dividend of 21 cents to be paid in early 2024 subject to the completion of the Canada transaction and necessary approvals. So our current strategy remains the best way to improve returns for our shareholders, and now I'll hand over to Georges.

GEORGES ELHEDERY, GROUP CHIEF FINANCIAL OFFICER: Thank you, Noel. Hello, everyone. Thank you for joining in person and via webcast today. I am glad to see many familiar faces, and I'm looking forward to meeting those of you I haven't had the opportunity to meet yet. Before I get into the Q4 numbers and given this is the first time I'm in front of you in this job, I'd like to share a few thoughts about my approach. You may know I've already spent 18 years with this firm running various businesses, including as CEO of the Middle East and most recently co-CEO of Global Banking and Markets, but what you may not know is that I spent most of this time creating efficiencies to achieve the purpose of investing in growth.

So indeed I oversaw the sale of non-strategic businesses in the Middle East, and this allowed us to focus our investments into Saudi Arabia and the United Arab Emirates, and when I led GB&M with Greg I drove the rationalisation of our product lines and booking structure to focus on areas where we had competitive advantage and could best serve our clients. So, as a result, I materially reduced RWAs and costs and repurposed those saves to invest in technology for the future of the business. I believe, therefore, that growth cannot be achieved without a clear focus on our strengths. Therefore, purposeful transformation and elimination of areas of marginal impact are paramount. Equally and as importantly, clinical delivery and keeping a tight grip on spending are key to unlocking the potential to invest.

So, as I approach this next phase, I want to emphasise my three focus areas: so, one, continuing to support our business to deliver growth and return, which is underpinned by continuing to improve customer service and attracting and retaining talent; number two is continuing to generate the further efficiencies required to support the investment I just spoke about; and number three, therefore the guiding principle that supports all of this, will be absolute cost and capital discipline.

I'll turn now to the Q4 numbers. Reported profits before tax were at $5.2 billion, up 95% on last year's fourth quarter. Adjusted profits before tax were at $6.8 billion, up 92%. Adjusted revenues were up 38%, driven mainly by net interest income growth of 53% and higher non-net interest income. We booked an expected credit loss charge of $1.4 billion in the quarter, and then adjusted costs were up 2% due to higher technology spend and higher performance-related pay. Compared to the previous quarter, lending and deposits were both down, but this was largely due to our banking operations in Canada being reclassified as held for sale. So, if you excluded this, lending was down 2% mainly due to subdued conditions in Hong Kong, and deposits were up.

For the full year, the dividend is at 32 cents per share with a second interim dividend of 23 cents per share. Also after strong capital generation and lower currency-adjusted RWAs our CET1 ratio was at 14.2%, an increase of 80 basis points on the third quarter. Our effective tax rate for 2022 was at 5%. This includes credit from the recognition of deferred tax assets related primarily in the UK as well as other deferred tax assets and uncertain tax position reassessments. If you excluded these credits, then the effective tax rate for 2022 was 19.2%, and we expect our normalised effective tax rate for 2023 to be around 20%.

This slide now shows another strong adjusted revenue performance, with overall growth of 38% compared to the fourth quarter of 2021, driven mostly by recent rate levels. There was strong growth in all businesses, as Noel indicated. Wealth and Personal Banking revenue was up 45%, Commercial Banking up 51% and Global Banking and Markets up 16%. Net fee income was down 11%. This was mainly due to, number one, lower wealth distribution revenue driven by lower equities turnover in Hong Kong in general and mutual fund sales, and this is reflecting soft equity markets in general; and, two, lower capital markets and advisory activity, which also impacted Global Banking and Markets.

On this slide, you can see that reported net interest income was at $9.6 billion, up 41% on last year's fourth quarter. The net interest margin was at 174 basis points, up 17 basis points on the third quarter of 2022 and up 55 basis points on the fourth quarter 2021. We continue to guide to a full-year 2023 net interest income of at least $36 billion on an IFRS 4 basis.

Let me unpack this a little bit. Our guidance, therefore, is unchanged to what we indicated at quarter three. We do view this as a conservative guidance, given current FX rate tailwinds and the strong fourth quarter performance, so this is why we're emphasising on 'at least $36 billion'. This is very important. There are a number of factors that we need to be aware of which is driving us to be conservative in our approach. The first one is the potential lag effect of customer migration to time deposits; the second one is the competitive pressures we may be facing in deposit pricing; and the third one is obviously the impact of foreign exchange and the future rates outlook. We do note consensus and we're not seeking to change it. We will be updating you on this NII performance throughout the year – I think at the Q1 results – when we will also incorporate the impact of IFRS 17 in our guidance.

We retain a cautious outlook on loan growth in the short term but continue to expect mid single-digit percentage annual loan growth in the medium-to-long term. Historically, our earnings have been very sensitive to short-term interest rate movements, and we have started to address this lately with additional structural hedging positions given the current rate levels. I will certainly update you later in the year on the progress towards this net interest income stabilisation or mitigation.

Turning to credit, our fourth quarter ECL charge was $1.4 billion, which includes $0.6 billion for our mainland China corporate real estate exposure. If you excluded this portfolio, the ECL charge was $0.8 billion or around 30 basis points of loans with limited signs of credit deterioration. So our main indicators therefore are still holding up. Given the macroeconomic headwinds, we expect an ECL charge of around 40 basis points for the full year 2022. Our ECL charge as a percentage of average loans includes loan balances held for sale from the planned sales of Canada and France retail. Therefore, when you exclude them, you need to add another four to five basis points on top of that number.

I do get a lot of questions on mainland China exposure, mainland China corporate real estate specifically, so in the spirit of transparency and having done lot of work on the dynamics of this portfolio, let me zoom in and walk you through that logic. First, our principal area of focus remains the portfolio booked in Hong Kong. The onshore portfolio is performing and the security is working. The exposure booked in Hong Kong reduced by around 20% in the second half of the year from $11.7 billion in Q2 to $9.4 billion, and this is primarily due to repayments. In Q4 we did see some further deterioration in that sector, so we looked at the portfolio again and decided to increase the share of sub-standard and credit-impaired exposures to around 16% of that portfolio. That's up from around 35% in Q2, and by doing so we increased our provisions accordingly.

So now, if you zoom in on the $6 billion exposure that we now raised as sub-standard or credit-impaired, $1.1 billion is secured with minimal ECLs due to the security held. So then against the remaining $4.9 billion we are holding $1.7 billion of provision, a circa 35% coverage ratio, and within this our coverage ratio against the unsecured credit-impaired exposure is around 55%. We also ran a number of downside scenarios, and I've included some of that analysis in the deck, which we can discuss in Q&A, if you wish to, but, to be clear, we did not need to factor those downside scenarios in the 31 December number, and since then our view of the sector has become more positive following the more accommodative policy stance that we've been seeing. So we are currently comfortable with our coverage level, but we will continue to monitor the situation very closely.

So I'll move on to costs now. Fourth quarter operating expenses were up 2% on the same period last year as most of the cost saves were broadly offset by technology spend and higher performance-related pay. The UK bank levy for 2022 was offset by credits from overpayments we made related to prior years. We expect an annual charge of around $200 million for 2023. Rebasing prior year costs at constant currency for hyperinflationary economies – that's specifically Turkey and Argentina – added around $200 million of cost growth to our adjusted cost base, so around half of the increase when you're comparing 2022 to 2021.

Our formal cost to achieve transformation programme, what we call the CTA programme, is now complete. We did achieve $5.6 billion of gross cost saves, which was somewhat at the top of our expectations, with an associated cost to achieve spend of $6.5 billion, which was towards the lower end of our guided range. As Noel said, we're still seeking and finding opportunities to create efficiencies that will deliver sustainable cost saves in future years. The costs thereof will be above the line. We're now considering up to $300 million of additional costs for severance in 2023. This will enable us to take out further management layers. These costs will be reported in our costs line.

Taking this into account, we're now aiming for approximately 3% cost growth in 2023, which remains a tough target in a high inflation environment. You should probably expect our 2023 costs to be marginally higher in Q1 as we're absorbing the run-down of the residual costs from the cost to achieve programme.

I'll move on to capital now, and the three points I wanted to call out here is, first, our CET1 ratio at 14.2%, up 80 basis points on the previous quarter. This is mainly due to an $8.5 billion capital benefit from higher profits and lower FX-adjusted underlying RWAs. Second, we're back in our CET1 ratio target operating range, which remains 14% to 14.5% for the medium term. The intention is to manage this range further down from medium to longer term and, given now we have returned to our target operating range six months earlier than we initially indicated, we have brought forward the consideration of future buybacks to the Q1 results.

And, finally, on the proceeds generated by the planned sale of our Canada banking operations, subject to the completion of the transaction, of course, we anticipate three potential uses: one, a special dividend of 21 cents per share, which will be the first priority use; two, we will consider additional buybacks over and above any existing buyback programmes; and, three, we will retain capital as required within the business, and we will update you on these later in the year.

Finally, on guidance, we are reiterating our guidance of at least $36 billion of net interest income for 2023. We remain on track to deliver a return on tangible equity of at least 12% from '23 onwards and, as I explained, we are now targeting approximately 3% cost growth in 2023. Our capital allocation target for Asia remains unchanged at 50%. Now, given the changes in the macroeconomic environment together with IFRS 17, we do not intend to continue to track insurance and fees as a percentage of group revenue nor Wealth and Personal Banking as a percentage of group tangible equity. Needless to say, these businesses remain absolutely strategically important and we remain absolutely committed to growing them.

In summary, this was a good set of results. We had revenue growth from all businesses, but we want to further increase and broaden revenues while protecting net interest income. We remain focused on meeting the needs of our customers through high quality propositions and our multi-channel international distribution network. As I said at the beginning, I have three focus areas: supporting the businesses to deliver growth and returns, continuing to generate further efficiencies and the strict cost and capital discipline.

Higher returns in 2023 would give us substantial distribution capacity in the future. A 50% dividend pay-out ratio has been established for 2023 and 2024. We will return to quarterly dividends from quarter 1. Considerations of buybacks have been brought forward to the quarter 1 results and we have signalled a 21 cents per share special dividend as the first priority use of proceeds generated by the planned sale of HSBC Canada, all followed by increased investment in growth and further buybacks in 2024 and 2025, subject of course to continued strong capital levels.

With that, I'll ask Richard to take us to Q&A. Thank you very much.

RICHARD O'CONNOR, GLOBAL HEAD OF INVESTOR RELATIONS: Thank you, operator, and good morning everyone. As per normal throughout these live events, we'll take a few questions from the floor to start with and then we'll go to the telephones and then coming back to the floor. As ever, please give your name and institution. Those in the auditorium, please wait for the mics to come around and please stick to a maximum of two questions per person and, if you've got more than that, we'll obviously try and come around again towards the end of the Q&A session.

With that, I'll start with Omar and then Martin.

OMAR KEENAN, CREDIT SUISSE: Good morning. Thank you for the presentation. I had questions on that net interest income piece. I was wondering if you could talk us a little bit through how the published rate sensitivities have changed versus what was published at the interim results. It looks like there's been some quite significant changes and it might be impacted by the NII stabilisation programme that you talked about. That would be really helpful.

And then my second question – just when we think about the recommencement of the buyback, given the good capital performance, when we think ahead to the first quarter how should we think about how you'll manage within the 14-14.5% range? Can we consider that any capital generation that lets the group land north of 14.5% might be, say, paid down to the mid-point, or something like that? But that would be quite helpful. Thanks.

NOEL QUINN: Thanks, Omar, and let me just give a couple of quick comments, before we go into the detail on rate sensitivity, just on NII because, just to reinforce some of the comments that Georges made, our guidance is unchanged quarter to quarter. I think it's important to keep it pretty consistent, but I do want to emphasise what Georges said. It's at least $36 billion. We do know the consensus is higher than $36 billion. The consensus currently is around $37 billion.

Georges said earlier, we're not looking to move consensus. We're comfortable with where consensus is. As Georges said, there are three factors that will play out over the next few weeks and months, and they are deposit migration, competitive pressures and foreign exchange. That will determine exactly what we mean by 'at least', but we'll update on that each quarter. I just want to reiterate: we're not looking to change consensus from its current level in the market.

And then on the rate sensitivity, Georges, do you want to just explain how that shift has taken place?

GEORGES ELHEDERY: Thanks, Noel. Thanks, Omar. So if you look at the downside 100 basis point shift we are reporting now $4 billion. You may have a record of $6 billion previously. The reduction is mainly due to two factors. Two-thirds of it is due to the rate level changing – obviously the higher the rate, the less you're compressed by the zero downside challenge –

and one-third is due to the additional structural hedging we have started putting on. We'd probably expect that one-third proportion to increase as we go forward.

To look at the upside, the number is $3.5 billion, 100 basis points up. I'd caution you that this number is somewhat theoretical, i.e. we're assuming 50% betas and no balance sheet change, so no deposit migration, etc. So we know that the real upside for higher rates will be lower than this. It will obviously be higher than where we are today, but lower than the $3.5 billion addition because you have to factor in a natural deposit migration and probably higher betas than 50% at the next juncture of rate increases.

On your second question, we're not giving an exact target. We're just stating a range: 14-14.5%. We're leaving it to our judgement and obviously the relevant approvals to assess what is excess capital beyond that 14%, but 14.5% is not necessarily the lower bound. It's a range, and therefore it's not a lower bound at which we judge excess capital.

MARTIN LEITGEB, GOLDMAN SACHS: Good morning. Could I just have one on NII and one on growth? Just in terms of net interest margin, a strong progression again quarter on quarter, both in Hong Kong, so HBAP, and the UK ring-fenced bank. I was just wondering could you give us a steer on how you think of the shape of net interest margins on these two core businesses going forward? Should we expect a broad picture of stability from here, in terms of hedge providing further tailwind, hopefully helping to offset migration, and would you expect the impact of deposit migration to be fairly front-end loaded into 2023 or could this be a longer term process?

And secondly, on growth, the improved and higher profitability outlook as we head into 2023 and some of the disposal proceeds from Canada being earmarked for growth and investment. I was just wondering, what growth opportunities are you most excited about and how to square that up with the guidance for low, single-digit growth this year? Thank you.

NOEL QUINN: Let me deal with the second one first and then Georges can come back and add any flavour on deposit migration. I think with the economic uncertainty that exists around the world at the moment, I think it's wise to be cautious on expecting too much underlying growth, particularly I think in the demand for term lending from corporates. I think they're in a cautionary mode at the moment. So that's why we're saying we're not expecting in the near term significant growth, particularly in the demand for term lending. I still think there's growth potential in working capital finance, trade. A lot will depend on global GDP.

That's why we've been a little bit more cautious near term, whilst also seeing that, once we get through those uncertainties, there'll be growth potential beyond that. What I'd also say, though: it's not equal. It's not even. We're seeing a very strong business performance in the Middle East at the moment. We're seeing good growth there. We're still gaining market share in mortgages. Granted, the market in the UK has shrunk for mortgages, probably around about 30%, but we're still seeking to grow market share and we can do so wisely and safely.

I'm still seeing very strong business activity levels in India. It's a strong market with good growth potential and Hong Kong has rebounded – not yet translating into demand for term lending from corporates, but we are seeing some early signs in January of Wealth activity starting to increase as the border with mainland China opened up and economic activity in Hong Kong opened. That's particularly focused more on investors willing to invest in the debt markets and structured products, rather than equity. I think they're waiting to see how the equity markets move forward.

We delivered $1 billion of adjusted profit in mainland China last year. So that's a good outcome and that was in a tough year. So I am expecting an economic rebound in mainland China. It will not be unaffected by the global slowdown. I think we're well-positioned, if there's growth in the world, through our Asia franchise, our international franchise and Middle East. We're well-positioned, but it's hard to predict exactly how much growth will be in the economy – so we've got to be a bit cautious.

In terms of linking it to Canada, we've been quite clear in our preferred use, our priority use, of the proceeds of Canada. The first priority use will be a special dividend of 21 cents and I think you can understand why we're doing that. The cancellation of the dividend for our retail shareholders was a significant event a few years ago and we want to try and put that right with the Canada transaction once that closes. The balance of the rest of the proceeds between retention and buyback, we haven't formed a view on at this point in time. We'll look at that, at the circumstances, when the Canada transaction closes. It will a combination probably of buyback and some retention, but I'm not giving guidance at this stage on what the balance is.

Georges, do you just want to add any further comments on NII? I'm going to reiterate, for the avoidance of doubt: we're not seeking to move guidance on NII. We tend not to give guidance on NIM.

GEORGES ELHEDERY: Thanks, Noel. Martin, a couple of comments that probably would help you figure it out. The first one is deposit migration and pass through is already happening, so we've already started to see it all the way from Q4. On that point, in Hong Kong the market tracks deposits, term deposits, we're substantially below the market, but we're tracking along the same direction. We've seen that the market in the UK – we've already increased our rates about seven times last year, so it kind of reflects this. So it is already happening.

The second thing I wanted to say is that we haven't seen such speed in rate hikes and such level of rates for a couple of decades now, which means however much we build and evaluate our forecast on expected customer behaviour and competitive pressures, we don't know, and this is why we wanted to stay somewhat conservative, but we are conservative for those reasons, to assess that. But, third, I think the proposition we have in both Hong Kong and the UK, since you called out these markets, is leading. Most of our customer deposits are transactional and operating accounts, which means we do expect stronger performance than what you may see as market numbers.

The one thing I just want to call out in Hong Kong to be mindful of is HIBOR, which is obviously a leading indicator of NII performance. Hong Kong has moved all the way to 5.3%, 5.4%, and dropped all the way to 2.4%, where I think they're on 2.9% today. There is a short-term headwind on NII due to that, but we believe it's only a short-term headwind due to inflows into Hong Kong and that will resolve itself.

NOEL QUINN: And I think that's a positive because what's happening in January, what we're seeing, is an inflow of capital back into Hong Kong, seeking opportunities for growth. That has temporarily, we believe, suppressed HIBOR a bit, but it's for a good reason not a bad reason.

AMAN RAKKAR, BARCLAYS: Morning. Hi, Noel. Hi, Georges. I've just got a question on revenue, principally around non-interest income. I think you're selling yourself a little bit short today around the revenue guidance. There's a lot of focus on net interest income and the $36 billion guide, but my understanding is that that includes a much bigger trading interest expense than the kind of numbers you were calling out in Q3. I think you told us to factor in a great than $1.3 billion drag in 2023, but it looks like that's annualising much north of $5 billion.

So it looks like the net interest income that you're calling out has a much bigger negative in it and I guess the assumption would be that there would be some positive trading income on that trading interest expense, which presumably is a big positive for non-interest income. I wouldn't want you to audit my spreadsheet, but I think I can get to a non-interest income number that's somewhere between $25 billion and $26 billion.

NOEL QUINN: As – I was going to say an ex-accountant. I don't think you're ever an ex-accountant, but – I'm probably not topical, but I like your double entry. So, yes, there's a double entry effect and Georges will explain the double entry.

GEORGES ELHEDERY: Your analysis is correct, is the short answer. Just to unpack it a little bit, the earnings from lending to the trading books in Global Banking and Markets are not booked in NII. They're booked in non-NII, due to the accounting. Those earnings for last year accounted for $2.5 billion in the non-NII line. Of that $2.5 billion, $1.3 billion was generated in Q4 – obviously with the rate level of Q4. With the assumption that the money the bank lends to the trading books in Global Banking and Markets stays where it is today and the rates stay where they are today, then it is not unreasonable to assume you can annualise the Q4 $1.3 billion for the full year 2023 and therefore, yes, you will be a couple of billion up year-on-year on the non-NII part, which is related to funding the trading books.

AMAN RAKKAR: So good analysis, fair observation and the – because non-interest income is a messy line – I know you've got IFRS 17 which you're going to come back to us on. Can you help us understand, year-on-year, the two big drivers of fee income, GB&M and Wealth Management? Is your best guess GB&M is up year-on-year? What's your best take on the underlying theme coming to the business year-on-year?

NOEL QUINN: First of all, on GB&M, I think we, as probably the market, have seen a strong level of activity in January. That's been particularly so in Debt Capital Markets, but we've seen a strong January. Will that sustain through the year is too early to predict, but good activity, good pipeline. On Wealth, I said earlier I think we're seeing some early signs of Wealth having a positive January in Hong Kong in particular. One should assume that positiveness should accelerate, but it's hard to know exactly by what rate, and I think equities will – equity investment will lag investment in the bond markets and the debt markets, but I think they're going to be the two drivers.

We're going to keep with the theme from growth in global payments and foreign exchange and trade. That's that bedrock that we had last year, that's grown around CAGRs of 6%, 7%, 8% per annum for the past three years will continue. We're not going to lessen our focus on that, but it should be supplemented by greater levels of activity in GB&M and in Wealth.

GEORGES ELHEDERY: We're not guiding towards fee income but, if you unpack it, every component of fee income is an area of strategic focus on growth so, subject to market conditions, you know where our investments are going, and fee income earning businesses are a clear priority, as Noel was indicating earlier.

ANDREW COOMBS, CITI: Thank you. I guess I'll carry on working down the P&L, so one on costs and one on provisions. Previously on the cost guidance, you talked about this $1 billion of cost saves at 3%, 5% inflation, net 2%, and now today there's the $300 million severance, taking you up to 3% cost growth. Just thinking more about the medium term, your messaging was 'no easing up on cost discipline and saves', but obviously the severance charges are somewhat lower than the CTA that you booked last year.

So, presumably, the attached cost savings are going to be lower than what you had as a tailwind following through into this year. So when we think about the cost base in the medium term and the underlying growth run rate, obviously inflation dependent, but do you see it slightly higher than 3% or do you think 3% is a medium term run rate?

NOEL QUINN: We're not giving guidance on 2024 costs at this point in time. I think it's too early. I think we've got to see where we go to on the inflation curve for the rest of the year. There's good progress on inflation, but it's still unpredictable. On your point, which I do want to come back on, our investment in technology continues. We're now at 20% of our total cost base in tech. That technology is improving customer propositions, but it's also improving processes, digitising processes more and more. We have a long-term programme of cost takeout over the future years – 2023, 2024 and 2025. That's already underway. From the IT investment that's already embedded in our plan, that will generate cost savings on a recurring basis as we digitise.

So I don't always need severance to get cost savings, because I've got IT investment to give me some cost savings and that is going to be continuing. Clearly, the more notice you have on that, the more ability you have to achieve that without severance because you can do natural attrition. Typically, the attrition rate in processing centres and in much of the cost base could be 10-15% per annum. Some places could be as high as 20% per annum attrition. So you have lead time ability to reposition your headcount without the need for severance as those processes are re-engineered, and we're going to be doing more of that going forward and therefore not have to call on things like CTA in the quantum we called on it in the past three years.

And I want to forget CTA. That's now history and we're just embedding cost savings as part of the fundamental architecture of the business going forward. Hopefully that's answered your question on cost.

ANDREW COOMBS: And then on provisions, thank you for providing the additional disclosure around Chinese commercial real estate. The $1 billion plausible downside that you provided on the Hong Kong booked Chinese commercial real estate positions, just so we have an understanding, you talk about that as plausible downside. Is that, or isn't that akin to your overall 40 basis points guidance? Is it the 40 that's the base case without that $1 billion?

NOEL QUINN: Let me give you an opening comment and then Georges can add some flavour. We ran that plausible downside as at 31 December without knowledge or the benefit of the positive policy moves that took place in January. So it's a like-for-like. We topped up the provisions. We thought the provisions were appropriate. We decided to do some scenario analysis. That's the result of the scenario analysis. We didn't think that scenario required to be provided against, or we would have put it in the balance sheet. We decided that was not required.

We had sufficient coverage, but we wanted to run a scenario that said, 'What is the plausible downside if things continue to get worse?' And that scenario, as existed in Q4, continued into 2023. Since then positive measures have happened, particularly the provision of liquidity to the offshore market and the rebooting of the China economy post-Covid. You could argue, in my terminology, that has changed the dynamics of that plausible downside – either the probability of it or the quantum of it – but we've not re-run it. It is what it was at 31 December.

What we try to give you is a scoping of what could happen if things continued the way they were. Now, I'm not going to answer the question, is it in the 40 basis points or isn't in the 40 basis points? We feel comfortable, whether it's looking at the global economy, our UK business, our Hong Kong business, China commercial real estate. We're guiding you to an overall ECL charge of around 40 basis points, the composition of which we're not going to blow out into any finer detail.

To the extent it's not needed for China real estate, for the plausible downside, it gives us more cover elsewhere. Is there any guide you want to add, Georges?

GEORGES ELHEDERY: I think you've already covered it exactly. Just to be very clear, it is a downside. It is not a forecast. We are very comfortable where we are now in terms of provisioning, and we have not factored $1 billion in the 40 basis points. So again, this is a downside. I think just zooming in on one thing, we have given you a grid to be able to do your own assessment. We have our own views on ECL from China real estate and the outlook, and how the sector can evolve, but we've unpacked the portfolio in a way that allows you to do your scenarios. You know what we've classified as sub-standard and credit impaired, and that's 60% of the optional portfolio. We've taken quite a robust view there.

You've seen the level of provisions we associated. If you wanted to increase in ECL coverage, you can come up with an equivalent scenario, and you can land on that plausible downside by just making your own assumptions about loss given default on these subsets of the portfolio.

GUY STEBBINGS, BNP PARIBAS EXANE: Hi. Morning, afternoon. Thanks very much for taking the questions, firstly on net interest income, and a quick follow-up on impairments. Firstly, in Hong Kong specifically, it's good NII mostly in the quarter, but you're flagging further negative deposit mix, HIBOR has drifted lower, and lending positions had been subdued. I'm just trying to get a sense, do you think, NII in Hong Kong specifically, should rise from Q1 run rate or whether we're capped up there or we need HIBOR to really recouple with US rates to get an NII to move from the Q4 run rate

And linked to that, in terms of deposit mix and deposit beta in your two largest markets, Hong Kong and the UK, you're obviously further headed in that journey in Hong Kong. Is the guidance from here predicated on a greater headwind coming in Hong Kong or UK when you think about deposit mix and beta specifically?

And then, just a quick follow-up on impairments. You've nudged up the guidance, and you now expect to be above normal. I appreciate your comments just now, that you don't want to get into all the detail in terms of composition there, but I just wondered if you can share any colour on which markets do you think there's a bit more of a risk about being above normalised cost of risk or, to put it another way, any markets you're incrementally more cautious since Q3 results? Thank you.

GEORGES ELHEDERY: Thank you, Guy. So on Hong Kong deposits, first, the HIBOR impact, we believe, is a short-term issue, and this is a correction, as Noel was explaining earlier, but you also have to look at what additional deposits this may mean for us. We're looking at this. Obviously, it's a headwind for NII. It's certainly a tailwind for the economic outlook of Hong Kong, its growth and the capability of growing the overall deposit and loan pool. So this is why we're yet to really see how the impact of the short-term HIBOR is going to be.

In terms of deposit mix – and this is valid for both Hong Kong and UK deposit mix and betas – this is happening already, as I did say. We are substantially better than the market averages that are reported, due to the nature of the deposits we have. They are mostly operating, transaction deposits, and we already factored in our guidance the fact that we will see additional, or a continuation of these migrations taking place. So we're very mindful that it will happen, and we're factoring it in.

The level of uncertainty we have is how much more or less, vis-à-vis, our own guidance is going to have. In the UK, as I said earlier, we've already increased rates seven times. You should expect that any 100-basis point higher from here will see marginally higher betas than the one we experienced before, but that's just the nature of how it will work, both for us and for the rest of the market. And that's exactly also how we're factoring in our guidance.

NOEL QUINN: The ECL risk, the obvious market that you maybe would ask questions on is the UK. We've talked a lot about China real estate, and I've already said that Southeast Asia is performing well, the Middle East is performing well. We have, principally in Europe, an international wholesale corporate book, and in the US, an international wholesale corporate book, so not exposed to retail credit pressures there. So that brings you to the UK, and I'll tell you, on the UK at the moment, we're not seeing any signs of stress at the moment of any significance outside of normality in UK retail banking. I think it's performing well. The mortgage book is holding up well. We're not seeing any major signs of stress in our book. I'm not saying the market isn't stressed, but I think in our book, we're comfortable. And we're much smaller in unsecured lending than many of our UK competitors, but again, we're not seeing any major signs of stress in the UK retail unsecured book.

It is fair to say that UK corporates, particularly smaller corporates to middle-market corporates, the inflationary pressures are having a negative impact on cashflow. But again, I'd say that's marginal deterioration in our book at the moment. It's not material deterioration. It's understandable pressures. So we're not seeing that turn in the corner into very negative territory at all at the moment.

Now, we'll have to see how that plays out for the rest of the year, but if I look at the 40 basis points, and you look at the pockets of where there are potential ECL charges could come from, we've given you a view on China real estate that says there's still a way to go for the China real estate market to get back to a level of normality, but it's turned the corner, and it's in positive territory. But there's still some way to go. So there's some potential usage of the 40 basis points there. There's some potential usage of the 40 basis points in the UK, but at the moment, it would be normal usage levels in the UK, which may be some possibly slightly higher usage levels in smaller to mid-market corporates, but it's marginal at the moment.

And then, the rest of the world are putting normal to positive territory. The Middle East is experiencing a very strong economy at the moment. So as I say, you could argue our normal range is between 30 and 40 basis points. We're trying to be a bit more cautious and position you at 40 basis points because of the uncertainty in the world.

TOM RAYNER, NUMIS SECURITIES: Good morning, Noel. Good morning, Georges. Can I maybe have another crack at trying to get you to comment on the medium-term cost guidance? If I take the guidance for 2023 of +3% and strip out the impact of the severance and the normalisation of the UK bank levy, and I strip out the billion dollars of flows through from previous cost savings, I think that 3% becomes more like an underlying 4% to 5%. Please correct me if you disagree. But my question would be, is 4% to 5% a fair view of what the underlying cost pressures are as we go into 2024, before any further incremental cost savings that may or may not come through, bearing in mind that –

NOEL QUINN: A nice try to get me to give you updated guidance on 2024! The one thing I will reiterate for you, though, just to help, we have programmes running that are part of business as usual, through digitisation, through technology, through simplification, process reengineering. You should expect that we will always have an element of cost savings coming through as part of continuing to drive efficiency, and I will use some of those cost savings to mitigate some of the inflationary impacts that exist in the environment. But I'm not going to quantify that trade-off between inflation and constant reengineering. But I think you're wrong to assume, in your arithmetic that you just had, that we've stopped trying to drive efficiency through. We will always try to drive some level of efficiency into the cost base as a mitigant against some of the inflation repressions.

So I wouldn't flow it all the way through, necessarily, into your models as a one-for-one calculation. But I'm not giving guidance at the moment on 2024 or 2025, other than cost discipline remains a core. Georges, do you want to add anything?

GEORGES ELHEDERY: I just want to just make sure you get the numbers right. So the bank levy benefit, i.e. the credit, is a 2022 benefit. We have said we are expecting normalisation of the bank levy to circa $200 million for 2023, and this is already baked into our cost guidance. So the benefit is past. It's in the 2022 1% number already, and we banked it, we knew it. And therefore, for 2023, you should strip it out. It's already in our cost guidance.

The second one is the cost saving flow through that will manifest this year in additional pay-related inflation of the overall pay pool. Again, as Noel indicated, when you're looking beyond 2023 you have to assess how the inflation outlook is during the course of 2023. We think the outlook is improving, and we think we've already baked into our pay the effect of the inflation that we've suffered, including double-digit jurisdiction inflation, etc. So that's not necessarily a repeat beyond 2023, at least not to the same extent.

I also want to just clarify the hyperinflation impact on cost is not budgeted. In our view, this is not a real cost growth. This is just an arithmetic growth that comes from rebasing prior year costs under our constant currency reporting. So therefore, we have not planned for this. We cannot manage it. Our view is this is not real cost growth, and we have not factored in. So it's just a clarification there.

JASON NAPIER, UBS: The first one, just focusing on the United States business and what's left of the North American franchise ex Mexico, the loan portfolio is really small, $54 billion, and the deposit box, about $100 billion. I appreciate a lot of the business that originated out of that region probably is booked elsewhere, but I just wondered in terms of the overhead that resides in that jurisdiction, the 75% cost-income that was delivered there last year, how you think about that and whether that's appropriately scaled for the shape of the business, going forward.

And then, secondly, the second question for me would be, on the capital walk, quite a lot of noise in the deductions in Q4. I just wanted to invite you perhaps to call out any changes from the Q4 end-of-period levels that we've got for things like DTAs and expected losses, and so on. Is there anything to flag in terms of headwinds to capital, following a very good print at the full-year stage? Thank you.

GEORGES ELHEDERY: Firstly, the cost-income ratio for North America, as Noel indicated, we're looking at the overall value of the franchise. We're looking at the income generated by those customers sitting in North America that booked specifically in East Asia and in the Middle East. So therefore, we're not commenting or managing specific legal entities' cost-income ratio. We will look at the profitability of clients, and we will look at the profitability of business lines and the returns of clients and the returns of business lines when we make these assessments.

On the capital work, so first, DTAs have been deducted from capital. At least the UK DTA, which was the substantial one, is gone as a significant item and therefore not in capital, and is also deducted from the dividend pay-out ratio. Other DTAs fall under the threshold deductions and get it. I don't think there's anything to worry about that. So therefore, I don't think we have any headwinds on capital as we go into Q1. It's just about the impact of profit generation, the impact of RWA growth for our CET1 ratio.

I may call it out here, just to make sure that I put your mind at ease, if this is coming through. Any impairment in BoCom, sitting under significant holdings, if it were to be needed, will result in virtually no CET1 ratio impact, again, due to those capital deductions, and therefore will result into no impact on our dividend pay-out and no impact to any share buy-back programme that may be running at such time of an impairment.

NOEL QUINN: Also, just on the US, I just want to say that Michael and the team in the US has done a great job in rationalising the portfolio. A lot of the actions they've taken in 2022 will have a full-year benefit in 2023. So I do expect the cost efficiency ratio of the US to come down from actions already taken, and he still sees further opportunities to rationalise the cost base of the US. So I think you'll see that ratio come down over time as you start to see full-year cost savings benefits hit into 2023. But he's done a great job in repositioning that portfolio over the past two to three years.

MANUS COSTELLO: Following up on the previous point about the revenue guidance. There is at least $2 billion of benefit year-over-year on non-interest income from the trading book impact. There were about a billion of one-off hits in non-interest income in 2022, and you've already said that net interest income, you're happy with the consensus being unchanged. So when I look at the revenue guidance for the year, it strikes me that – or the revenue consensus for the year, I should say, it strikes me that the revenue consensus is at least a couple of billion too low.

I wondered if you were able to comment on that, because there's some confusion, I think, that there's a revenue downgrade coming out of this set of earnings which, based on the comments you've made so far on this call, doesn't seem to me to be the right conclusion. Thank you.

GEORGES ELHEDERY: Thank you, Manus. Your analysis is correct. The first one is there's indeed a couple of billion that you need to factor in in the non-NII due to the funding of the trading book, assuming roughly flat balances and flat rates throughout 2023 to the Q4 number. So, yes, that one's correct.

The second one is, yes, the fee income has been subdued in 2022, particularly in Wealth. And we explained the situation in Hong Kong earlier, as well as in the Capital Markets and Advisory activities in Global Banking and Markets, both of which do seem to reverse. At least the first month of this year has been much more optimistic. We've seen a resumption of activity in Wealth.

Now, I can't comment on the quantum of the reversal of that lost income last year, but your assessment is fair. Now, all in all, I cannot guide to non-NII, but I think the ingredients you have here are fair to be used.

NOEL QUINN: Thank you very much for all of your questions and your time. To close with a few comments, we've completed the first phase of our transformation. Our international connectivity remains our greatest strength, and it's now underpinned by good, broad-based profit generation. That's a powerful combination. You can see it in the strong delivery in 2022. We've also got a tight grip on costs, and we're on track to deliver our returns target, but there's so much more we can do. We're well positioned to further improve growth and returns, and we expect to have substantial distribution capacity for dividends, buybacks and potentially a special dividend in early 2024.

Richard and the team are available to you if you have any further questions, but in the meantime, have a good afternoon or morning, and thank you for being with us.