

GRUPO FINANCIERO HSBC MEXICO, S. A. DE C.V.
Sociedad Controladora Filial
AND SUBSIDIARIES

Consolidated Financial Statements

December 31, 2014 and 2013

(With Independent Auditors' Report Thereon)

(Translation from Spanish Language Original)



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Independent Auditors' Report

(Translation from Spanish language original)

The Board of Directors and Stockholders
Grupo Financiero HSBC, S. A. de C. V.,
Sociedad Controladora Filial and Subsidiaries:

We have audited the accompanying consolidated financial statements of Grupo Financiero HSBC, S. A. de C. V., Sociedad Controladora Filial and Subsidiaries (the Group), which comprise the consolidated balance sheets as at December 31, 2014 and 2013 and the consolidated statements of income, changes in stockholders' equity and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and presentation of these consolidated financial statements in accordance with the accounting criteria for financial group holding companies in México, established by the National Banking and Securities Commission (the Banking Commission), and for such internal control as Management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the Group's preparation and presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by Management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

(Continued)

Opinion

In our opinion, the consolidated financial statements of Grupo Financiero HSBC, S. A. de C. V., Sociedad Controladora Filial and Subsidiaries for the years ended December 31, 2014 and 2013 have been prepared, in all material respects, in accordance with the accounting criteria for financial group holding companies in Mexico issued by the Banking Commission.

KPMG CARDENAS DOSAL, S. C.



Hermes Castañón Guzmán

February 11, 2015.



GRUPO FINANCIERO HSBC, S. A. DE C. V.,
Sociedad Controladora Filial
AND SUBSIDIARIES

Consolidated Balance Sheets

December 31, 2014 and 2013

(Millions of pesos)

Assets	2014	2013	Liabilities and Stockholders' Equity	2014	2013
Cash and cash equivalents (note 6)	\$ 40,690	55,407	Deposit funding:		
Margin accounts (note 7)	7	-	Demand deposits (note 20)	\$ 177,230	178,070
Investment securities (note 8):			Time deposits: (note 20):		
Trading	55,004	58,568	General public	92,680	103,414
Available-for-sale	132,527	96,081	Money Market	22,474	-
Held-to-maturity	32,002	16,773	Bank bonds (note 21)	6,233	6,036
	219,533	171,422		298,617	287,520
Debtors under agreements to resell (note 9)	-	500	Due to banks and other institutions		
Derivatives (note 11):			(notes 12c and 22):		
Trading	79,964	49,601	On demand	13,765	2,900
Hedging	77	168	Short-term	26,088	15,466
	80,041	49,769	Long-term	2,168	2,144
Current loan portfolio (note 12):			Technical reserves (note 23)	12,253	11,432
Commercial loans:			Creditors under agreements to repurchase (note 9)	60,247	34,765
Commercial activity	114,574	108,207	Collateral sold or pledged as guarantee (note 10):		
Financial institutions	9,878	4,339	Repurchase	11	-
Government institutions	32,541	18,133	Securities lending	21,886	9,076
Consumer loans	36,371	37,675		21,897	9,076
Residential mortgages	25,853	24,480	Derivatives (note 11):		
Total current loan portfolio	219,217	192,834	Trading	80,049	46,853
Past due loan portfolio (note 12):			Hedging	1,230	790
Commercial loans:				81,279	47,643
Commercial activity	10,017	9,617	Accounts payable to reinsurers		
Financial institutions	-	3	and bonding	10	13
Government institutions	85	45	Other accounts payable:		
Consumer loans	1,568	1,788	Income tax and employee statutory		
Residential mortgages	573	703	profit sharing (note 27)	165	954
Total past due loan portfolio	12,243	12,156	Settlement transactions creditors (note 14)	16,868	37,659
Total loan portfolio	231,460	204,990	Sundry creditors and other accounts		
Less:			payable (note 24)	15,355	15,137
Allowance for loan losses (note 12d)	12,693	12,223		32,388	53,750
Loan portfolio, net	218,767	192,767	Subordinated debt issued (note 26)	10,144	9,463
Benefits receivable on securitization			Deferred credits	710	599
transactions (note 12c)	147	182		10,854	10,062
Premium debtors, net	36	53	Total liabilities	559,566	474,771
Accounts receivable from reinsurers,			Stockholders' equity (note 28):		
net (see note 13)	59	73	Paid-in capital:		
Accounts receivable from insurance and bonding			Capital stock	5,637	5,637
institutions (see note 13)	58	18	Additional paid-in capital	32,186	32,186
Other accounts receivable, net (note 14)	34,834	40,404		37,823	37,823
Foreclosed assets, net (note 15)	73	159	Earned capital:		
Property, furniture and equipment, net			Statutory reserves	2,445	2,259
(note 16)	6,146	6,927	Retained earnings	11,215	11,489
Equity investments			Unrealized gain from valuation of		
(note 17)	239	234	available-for-sale securities	489	290
Long-term assets available for sale (note 18)	-	35	Mark to market from cashflow hedges	(26)	(9)
Deferred income taxes and deferred employee			Subsidiary dilution effect	199	199
statutory profit sharing, net (note 27)	8,710	7,710	Net income	1,981	3,714
Other assets, deferred charges and intangible				16,303	17,942
assets (notes 19 and 24)	4,357	4,880	Non-controlling interest	5	4
			Total stockholders' equity	54,131	55,769
			Commitments and contingent liabilities (note 32)		
Total assets	\$ 613,697	530,540	Total liabilities and stockholders' equity	\$ 613,697	530,540

(Continued)

**GRUPO FINANCIERO HSBC, S. A. DE C. V.,
Sociedad Controladora Filial
AND SUBSIDIARIES**

Consolidated Balance Sheets, continued

December 31, 2014 and 2013

(Millions of pesos)

Memorandum accounts

	<u>2014</u>	<u>2013</u>
Transactions in custody	\$ 58,973	43,724
Loan commitments (notes 12 and 30a)	33,874	25,561
Assets in trust or under mandate (note 30b)	458,166	439,469
Assets in custody or under management (note 30d)	436,545	341,218
Collaterals received by the entity (note 8)	21,979	17,291
Collaterals received by the entity and sold or pledged in guarantee (note 8)	21,897	16,583
Investment banking transactions on behalf of customers, net (note 30c)	46,233	50,353
Uncollected interest accrued in respect of overdue credit portfolio (note 12c)	276	221
Amounts under derivative instruments	3,367,817	2,771,506
Loan portfolio rated (note 12)	265,334	230,551
Other memorandum accounts	<u>341,535</u>	<u>326,413</u>

See accompanying notes to the consolidated financial statements.

"These balance sheets consolidated with those of financial entities and other companies that are part of the Financial Group that are susceptible to consolidation, were formulated in accordance with the accounting criteria for financial group holding companies, issued by the National Banking and Securities Commission, based on the provisions of Article 30 of the Financial Group Regulating Law, of general and mandatory observance, and all the operations conducted by the Controlling Company and all financial entities and other companies that are part of the Financial Group susceptible to consolidation are reflected through the dates mentioned above, which were conducted and valued based on sound banking practices and on the applicable legal and administrative provisions."

"These consolidated balance sheets were approved by the Board of Directors under the responsibility of the undersigned officers."

"At December 31, 2014 and 2013, the nominal capital stock of Grupo Financiero HSBC amounts to \$5,637."

SIGNATURE

Luis Peña Kegel
Chief Executive Officer

SIGNATURE

Gustavo Ignacio Méndez Narváez
Chief Financial Officer

SIGNATURE

David Chrichton Meechie
Director of Internal Audit

SIGNATURE

Juan José Cadena Orozco
Chief Accountant

**GRUPO FINANCIERO HSBC, S. A. DE C. V.,
Sociedad Controladora Filial
AND SUBSIDIARIES**

Consolidated Statements of Income

Years ended December 31, 2014 and 2013

(Millions of pesos)

	<u>2014</u>	<u>2013</u>
Interest income (note 31a)	\$ 30,402	30,991
Premiums income, net	2,893	3,030
Interest expense (note 31a)	(8,876)	(9,370)
Net increase in technical reserves (note 23)	(702)	(890)
Claims and other contractual obligations	<u>(1,761)</u>	<u>(1,169)</u>
Financial margin (note 31a)	21,956	22,592
Allowance for loan losses (note 12d)	<u>(8,002)</u>	<u>(8,086)</u>
Financial margin net of allowance for loan losses	13,954	14,506
Commission and fee income (note 12c)	8,296	8,711
Commission and fee expense	(1,715)	(1,802)
Financial intermediation income (note 31b)	1,590	2,420
Other operating income (note 31c)	2,405	2,530
Administrative and promotional expenses	<u>(22,214)</u>	<u>(21,702)</u>
Net operating income	2,316	4,663
Equity in the results of associated and affiliated companies, net (note 17)	<u>49</u>	<u>43</u>
Income before income taxes	2,365	4,706
Current income taxes (note 27)	(1,005)	(2,244)
Deferred income tax (note 27)	<u>735</u>	<u>1,067</u>
Income before from discontinued operations	2,095	3,529
Discontinued operations (note 18)	<u>(113)</u>	<u>186</u>
Income before non-controlling interest	1,982	3,715
Non-controlling interest	<u>(1)</u>	<u>(1)</u>
Net income	<u>\$ 1,981</u>	<u>3,714</u>

See accompanying notes to the consolidated financial statements.

"These statements of income consolidated with those of the other financial entities and other companies that are part of the Financial Group, were formulated in accordance with the accounting criteria for financial group holding companies, issued by the National Banking and Securities Commission, based on the provisions of Article 30 of the Financial Group Regulating Law, of general and mandatory observance, and all the revenues and expenses from the operations conducted by the Controlling Company and all financial entities and other companies that are part of the Financial Group susceptible to consolidation are reflected through the years mentioned above, which were conducted and valued based on sound banking practices and on the applicable legal and administrative provisions".

"These consolidated statements of income were approved by the Board of Directors under the responsibility of the undersigned officers".

SIGNATURE

Luis Peña Kegel
Chief Executive Officer

SIGNATURE

Gustavo Ignacio Méndez Narváez
Chief Financial Officer

SIGNATURE

David Chrichton Meechie
Director of Internal Audit

SIGNATURE

Juan José Cadena Orozco
Chief Accountant

GRUPO FINANCIERO HSBC, S. A. DE C. V.,
Sociedad Controladora Filial
AND SUBSIDIARIES

Consolidated Statements of changes in Stockholders' Equity

Years ended December 31, 2014 and 2013

(Millions of pesos)

	Paid-in capital		Earned capital					Net income	Non-controlling interest	Total stockholders' equity
	Capital stock	Additional paid-in capital	Capital reserves	Retained earnings	Unrealized gain (loss) from available-for-sale securities	Mark to market from cashflow hedges	Subsidiary dilution effect			
Balances at December 31, 2012	\$ 5,111	27,562	1,958	8,833	902	(103)	199	6,016	11	50,489
Changes resulting from stockholder resolutions (note 28a):										
Resolution at the Ordinary General Stockholders' Meeting on January 24, 2013 - Increase in Capital stock and additional paid-in capital	526	4,624	-	-	-	-	-	-	-	5,150
Resolution at the Ordinary General Stockholders' Meeting on April 26, 2013 - Reserve constitution	-	-	301	5,715	-	-	-	(6,016)	-	-
Resolution at the Board of Director's Meeting on March 21, 2013 - Dividends paid from the resolution made on March 26, 2013	-	-	-	(2,500)	-	-	-	-	-	(2,500)
Total items related to stockholders' resolutions	526	4,624	301	3,215	-	-	-	(6,016)	-	2,650
Changes related to the recognition of comprehensive income (note 28b):										
Net income	-	-	-	-	-	-	-	3,714	-	3,714
Valuation effect of available-for-sale securities and cashflow hedges (notes 8 and 11)	-	-	-	-	(612)	94	-	-	-	(518)
Recognition of the effect derived from the application of the new methodology for determining the allowance for commercial loan losses, recognized in retained earnings (note 3)	-	-	-	(559)	-	-	-	-	-	(559)
Non-controlling interest	-	-	-	-	-	-	-	-	(7)	(7)
Total comprehensive income	-	-	-	(559)	(612)	94	-	3,714	(7)	2,630
Balances at December 31, 2013	5,637	32,186	2,259	11,489	290	(9)	199	3,714	4	55,769
Changes resulting from stockholder resolutions (note 28a):										
Resolution at the Ordinary General Stockholders' Meeting on April 28, 2014 - Reserve constitution	-	-	186	3,528	-	-	-	(3,714)	-	-
Resolution at the Ordinary General Stockholders' Meeting on March 28, 2014 - Dividends paid	-	-	-	(3,781)	-	-	-	-	-	(3,781)
Total items related to stockholders' resolutions	-	-	186	(253)	-	-	-	(3,714)	-	(3,781)
Changes related to the recognition of comprehensive income (note 28b):										
Net income	-	-	-	-	-	-	-	1,981	-	1,981
Valuation effect of available-for-sale securities and cashflow hedges (notes 8 and 11)	-	-	-	-	199	(17)	-	-	-	182
Recognition of the effect derived from the application of the new methodology for determining the allowance for commercial loan losses, recognized in retained earnings (note 4a)	-	-	-	(21)	-	-	-	-	-	(21)
Non-controlling interest	-	-	-	-	-	-	-	-	1	1
Total comprehensive income	-	-	-	(21)	199	(17)	-	1,981	1	2,143
Balances at December 31, 2014	\$ 5,637	32,186	2,445	11,215	489	(26)	199	1,981	5	54,131

See accompanying notes to the consolidated financial statements.

"These consolidated statements of changes in stockholders' equity were formulated in accordance with the accounting criteria for financial group holding companies, issued by the National Banking and Securities Commission, based on the provisions of Article 30 of the Financial Group Regulating Law, of general and mandatory observance, applied consistently, and all changes in the stockholders' equity account from the operations conducted by the Financial Group through the years ended on the dates mentioned above, which were conducted and valued based on sound banking practices and on the applicable legal and administrative provisions."

"These consolidated statements of changes in stockholders' equity were approved by the Board of Directors under the responsibility of the undersigned officers".

SIGNATURE
Luis Peña Kegel
Chief Executive Officer

SIGNATURE
Gustavo Ignacio Méndez Narváez
Chief Financial Officer

SIGNATURE
David Chrichton Meechie
Director of Internal Audit

SIGNATURE
Juan José Cadena Orozco
Chief Accountant

**GRUPO FINANCIERO HSBC, S. A. DE C. V.,
Sociedad Controladora Filial
AND SUBSIDIARIES**

Consolidated Statements of Cash Flows

Years ended December 31, 2014 and 2013

(Millions of pesos)

	<u>2014</u>	<u>2013</u>
Net income	\$ 1,981	3,714
Adjustments for non cash items:		
Depreciation of property, furniture and equipment	1,344	1,274
Amortization of intangible assets	407	389
Technical reserves	702	890
Provisions	1,557	2,655
Current and deferred income taxes	270	1,671
Equity in the results of associated and affiliated companies	(49)	(43)
Non-controlling interest	1	1
Discontinued operations	(113)	(186)
	<u>6,100</u>	<u>10,365</u>
Operating activities:		
Change in margin accounts	(7)	53
Change in investment securities	(47,747)	(16,138)
Change in debtors under agreements to resell	500	7,206
Change in derivatives (assets)	(30,276)	(6,287)
Change in loan portfolio	(26,031)	(3,968)
Changes in premium debtors (net)	17	16
Changes in receivables from insurance and bonding institutions (net)	(40)	(16)
Change in reinsurers and re-guarantee (net)	14	44
Change in foreclosed assets	86	59
Change in other operating assets	6,146	(7,823)
Change in deposit funding	11,098	(7,805)
Change in loans from banks and other institutions	21,511	(2,217)
Change in creditors under agreements to repurchase	25,482	14,036
Change in collateral sold or pledged as guarantee	12,820	5,188
Change in derivatives (liability)	33,635	6,722
Change in reinsurers and re-guarantee (net) (liability)	(4)	(1)
Change in subordinated debt issued with liability characteristics	681	(733)
Change in other operating liabilities	(21,863)	2,580
Income taxes paid	(2,157)	(2,514)
Net cashflows from operating activities	<u>(10,035)</u>	<u>(1,233)</u>
Investing activities:		
Proceeds from sale of property, furniture and equipment	-	3
Purchase of property, furniture and equipment	(648)	(997)
Proceeds from associated and affiliated companies	-	130
Purchase of intangible assets	(266)	(1,026)
Proceeds from dividends in cash	37	34
Proceeds from disposal of long-lived assets available for sale	1	-
Others	(25)	-
Net cashflows from investing activities	<u>(901)</u>	<u>(1,856)</u>
Financing activities:		
Increase in Capital stock and additional paid-in capital	-	5,150
Payment of dividends	(3,781)	(2,500)
Net cash flows from financing activities	<u>(3,781)</u>	<u>2,650</u>
Net decrease in cash and cash equivalents	(14,717)	(439)
Cash and cash equivalents at the beginning of year	<u>55,407</u>	<u>55,846</u>
Cash and cash equivalents at end of year	<u>\$ 40,690</u>	<u>55,407</u>

See accompanying notes to the consolidated financial statements.

"These consolidated statements of cash flows, were formulated in accordance with the accounting criteria for financial group holding companies, issued by the National Banking and Securities Commission, based on the provisions of Article 30 of the Financial Group Regulating Law, of general and mandatory observance, and all incoming and outgoing cash flows from the operations conducted by the institution through the years mentioned above are reflected, which were conducted and valued based on sound banking practices and on the applicable legal and administrative provisions."

"These consolidated statements of cash flows were approved by the Board of Directors under the responsibility of the undersigned officers".

SIGNATURE
Luis Peña Kegel
Chief Executive Officer

SIGNATURE
Gustavo Ignacio Méndez Narváez
Chief Financial Officer

SIGNATURE
David Chrichton Meechie
Director of Internal Audit

SIGNATURE
Juan José Cadena Orozco
Chief Accountant

GRUPO FINANCIERO HSBC, S. A. de C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

For the years ended December 31, 2014 and 2013

(Millions of pesos)

These consolidated financial statements have been translated from the Spanish language original solely for the convenience of foreign/English-speaking readers.

(1) Description of business and significant transactions-

Description of business-

Grupo Financiero HSBC, S. A. de C. V., Sociedad Controladora Filial (the Group) is a subsidiary of HSBC Latin America Holdings (UK) Limited, domiciled in Paseo de la Reforma 347, Colonia Cuauhtémoc, Z. C. 06500, Delegación Cuauhtémoc, Mexico City., who owns 99.99% of its capital stock and is authorized to purchase and manage voting stock issued by financial entities, stock market firms, special purpose financial intermediaries, as well as those companies that provide complementary or ancillary services predominantly to one or more of these financial entities.

As of December 31, 2014 and 2013, the Financial Group and its consolidated subsidiaries include: (i) HSBC México, S. A., Institución de Banca Múltiple, Grupo Financiero HSBC and subsidiaries (the Bank) which is a commercial banking institution whose operations include, among others, accepting deposits, granting loans, securities and derivatives transactions and entering into trust contracts; (ii) HSBC Casa de Bolsa, S. A. de C. V. (the Brokerage Firm) that acts as a financial intermediary in authorized securities transactions, (iii) HSBC Global Asset Management (México), S. A. de C. V. (the Asset Manager), which provides administrative and operating services to investment companies managed by the Financial Group; (iv) HSBC Servicios, S. A. de C. V. (HSBC Servicios), which provides advisory services related to financial systems, including consulting and technical assistance in administrative processes; (v) HSBC Seguros, S. A. de C. V. and subsidiaries (the Insurance Company, entity regulated by the National Insurance and Bonding Commission (Insurance and Bonding Commission), which main objective is to engage, in terms of the General Law of Mutual Insurance Institutions and Companies (the LGISMS), in insurance, coinsurance and reinsurance activities, and (vi) through December 31, 2013, HSBC Fianzas, S. A. (the Bonding Company, entity regulated by the Insurance and Bonding Commission), which objective was to issue bonds in terms of the Federal Bonding Institution Law (LFIF) (note 18). The above entities, except for the Insurance Company and the Bonding Company are regulated by the National Banking and Securities Commission (the Banking Commission) and other applicable laws.

Significant transactions and other issues-

2014

During December 2014, the Financial Group throughout the Bank placed six issuances of Bonds (CEDES) amounting to \$22,450, bearing monthly interest at the Interbank Equilibrium Interest Rate (TIE for its acronym in Spanish language) with an expiring date between March and June of 2015 (note 20).

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

2013

On August 21, 2013, the Financial Group entered into a contract to sell the Bonding Company to Afianzadora Aserta, S. A. de C. V. Grupo Financiero Aserta subject to the authorization from the corresponding authorities. As explained in note 18, this transaction was authorized on December 13, 2013.

On December 9, 2013, the Group throughout the Bank placed two issuances of Bonds (CEBURES); the first issuance aggregating to \$2,300 with a 5-year term, bearing monthly interest at the THIE rate plus 30 basis points and the second issuance to \$2,700, with a 10-year term, bearing half-yearly interest at the rate of 8.08% (note 21).

On January 31, 2013, the Group throughout the Bank issued preferred subordinated debentures, subject to mandatory conversion into common shares representing capital stock, provided that any of the following conditions is met: (i) where the result from dividing the Tier 1 Basic Capital by the Bank's total weighted assets subject to risk is 4.5% or less; or (ii) where the Banking Commission notifies the Bank that it has not complied with the minimum remedial action in case of not having the minimum capitalization level required or when non complying with the minimum capitalization index required by the Law of Credit Institutions (LIC) and the Bank does not rectify such situation. Such issuance totaled US\$110 million and bears interest at the 30-day LIBOR rate plus 3.65 basis points (note 26).

(2) Authorization and basis of presentation-

Authorization

On February 11, 2015, Luis Peña Kegel (Chief Executive Officer), Gustavo Ignacio Méndez Narváez (Chief Financial Officer), David Chrichton Meechie (Director of Internal Audit) and Juan José Cadena Orozco (Chief Accountant) authorized the issuance of the accompanying consolidated financial statements and related notes thereto.

In accordance with the General Corporations Law and the Group's bylaws, the stockholders are empowered to modify the financial statements after issuance. The unconsolidated financial statements issued on the same date, will be submitted for approval at the next Stockholders' Meeting.

Basis of preparation

a) Statement of compliance

The accompanying consolidated financial statements have been prepared in conformity with the accounting criteria for financial group holding companies in Mexico issued by the Banking Commission (the Accounting Criteria), which were in effect at the consolidated balance sheet date. The Banking Commission is responsible for the inspection and supervision of credit institutions and for reviewing their financial information.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

The financial statements of subsidiaries have been prepared in conformity with the accounting criteria established by the Banking Commission, except for the financial statements of the Insurance Company, which have been prepared in conformity with the accounting criteria for insurance institutions in Mexico, issued by the Insurance and Bonding Commission.

The Accounting Criteria states that if there is a lack of specific accounting criterion from the Banking Commission for credit institutions, or in a broader context of Mexican Financial Reporting Standards (FRS), the supplementary basis under FRS A-8 should be applied, and only if the International Financial Reporting Standards (IFRS for its acronym in English) as referred to in the FRS A-8, do not provide solutions to the accounting recognition, a suppletory norm could be applied, only if it complies with all requirements mentioned in the aforementioned FRS, and under the following order: the accounting principles generally accepted in the United States of America (US GAAP) and any accounting criterion that forms part of a formal and recognized accounting criteria.

b) Use of estimates and judgments

The preparation of consolidated financial statements requires management to make a number of estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities as of the date of the financial statements and the reported amount of revenues and expenses during the reporting period. Significant items subject to such estimates and assumptions include the carrying value of investment securities and derivatives, repos, securities lending, allowance for loan losses, foreclosed assets, technical reserves, employee retirement benefits and deferred income taxes. Actual results may differ from these estimates and assumptions.

c) Functional and reporting currency

The aforementioned consolidated financial statements are presented in Mexican pesos (reporting currency), which is the same as the local and the functional currency.

For purpose of disclosure in the notes to the consolidated financial statements, when reference is made to pesos or "\$", it means millions of Mexican pesos, and when referring to USD\$ or dollars, means dollars of the United States of America.

d) Recognition of assets and liabilities related to purchase and sale of foreign currencies and derivative financial instruments

The consolidated financial statements of the Group recognize assets and liabilities related to purchase and sale of foreign currencies, investment securities, repurchase agreements securities lending and derivative financial instruments at the date when transactions are made, regardless of the settlement date.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos, excluding the value of the UDI)

(3) Summary of significant accounting policies-

The significant accounting policies applied in the preparation of the consolidated financial statements are as follows:

(a) Recognition of the effects of inflation-

The accompanying consolidated financial statements include the recognition of the effects of inflation on the financial information until December 31, 2007, the date on which according to the FRS B-10 "Effects of Inflation" the economy changed from an inflationary to a non inflationary environment (cumulative inflation in the last three years less than 26%), using for this purpose the Investment Unit Value (UDI for its acronym in Spanish). The UDI is a unit of measurement whose value is determined by the "Banco de México" (Central Bank) based on inflation. The accumulated annual inflation percentages of the three preceding years and the UDI values at the end of indicated years are as follows:

<u>December 31</u>	<u>Inflation</u>		
	<u>UDI</u>	<u>Annual</u>	<u>Accumulated</u>
2014	5.2704	4.18%	12.34%
2013	5.0587	3.77%	11.76%
2012	4.8746	3.90%	12.31%
	=====	=====	=====

(b) Basis of consolidation-

The accompanying consolidated financial statements include those of the Group and those of its subsidiaries, including the special purpose entity (SPE) that qualifies to be consolidated in accordance with the accounting criteria. Significant intercompany transactions and balances have been eliminated in consolidation. The consolidation was made based on the financial statements of the subsidiaries as of and for the years ended December 31, 2014 and 2013, except for the financial statements of the SPE, which have been prepared as of and for the twelve-month periods ended November 30, 2014 and 2013, without any relevant transactions in the non-coinciding period. In the following pages are detailed the subsidiaries, SPE, and the percentage of the shareholding of the Group as at December 31, 2014 and 2013.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

<u>Subsidiary</u>	<u>Shareholding percentage</u>
Bank	99.99%
Brokerage Firm	100.00%
Operating company	100.00%
HSBC Servicios	100.00%
Insurance Company	100.00%

The controlling interest includes the direct and indirect interest of the Group in its subsidiaries.

Special Purpose Entity (SPE)

As of December 31, 2014 the Bank has incorporated the following SPE, which has been consolidated in the Bank's financial statements and consequently in the Group's, given that the Bank has the control and it was created to achieve a specific purpose.

- Irrevocable administrative trust 1052 created in April 2011 upon the execution of the acknowledgment of debt and payment between the Bank and Hipotecaria Su Casita, S. A. de C. V., SOFOM ENR, arising from a loan granted by the Bank. As a result of the aforementioned, the Bank is the owner of "patrimonio A" which consists of: a) individual loans with mortgage guarantee ("capital loans"); b) cash furniture and real estate properties reserved as part of the trust management and credit collection; and, c) collection rights arising from capital loans. As of December 31, 2014 and 2013, "patrimonio A" amounts to \$260 and \$336, respectively, which is included under the "Residential Mortgages loans" item in the consolidated balance sheet.

On March 22, 2013, the operations of the following SPE were early terminated:

- Joint venture created between Credit Suisse Capital Partners (Luxembourg) S.à.r.l., the Bank, and Credit Suisse Alzette Holdings S.à.r.l. (Tula), incorporated in June 2011, where the Bank had an interest of 99.3% of the risks and benefits of the assets and liabilities, which purpose was the investment in high credit rating debt denominated in pesos. The effects and transactions in force at the date of the early termination were incorporated in the Bank's own operations as part of investments in securities, classified as available-for-sale as of December 31, 2013 and until January 23, 2014, date when these were sold.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

(c) *Cash and cash equivalents-*

Cash and cash equivalents consist of cash, precious metals (coins), bank account balances, 24 and 48-hour foreign currency purchase and sale transactions, bank loans with original maturities of up to three days ("Call Money") and deposits with the Central Bank.

Offsetting entries for 24 and 48-hour foreign currency purchase and sale transactions represent rights or obligations, which are recorded in "Other accounts receivable, net" and "Settlement transactions", respectively.

This category includes deposits related to monetary regulation, as required by the Law of the Central Bank, whose purpose is regulating the liquidity of the money market and are recognized as a restricted asset.

At the date of the consolidated financial statements, interest income and profit or losses on valuation are included in the income statement as incurred as part of the interest income or interest expense. Moreover, results from valuation and sale of precious metal coins and currency are grouped in the consolidated statement of income under the caption "Financial intermediation income".

(d) *Margin accounts-*

This account is comprised of the total collateral held in cash, securities or other highly liquid instruments in respect of derivative transactions on recognized stock market exchanges.

(e) *Investment securities-*

Investment securities consist of equities, government, bank and corporate securities, listed and unlisted, classified into the next categories, depending on management's investment intentions.

Trading securities-

Trading securities are bought and held mainly to be sold to obtain gains due to price differences in the short term purchase and sale transactions. Debt securities and equities are initially and subsequently marked to market at a price provided by an independent price vendor. Valuation effects are recognized in results of operations within "Financial intermediation income". If the amount of trading securities is short for settling the amount of securities deliverable in value date transactions in relation to purchase-and-sale of securities, the credit balance is shown as a liability under "Delayed delivery securities".

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

Available-for-sale securities-

Securities not classified as trading or held-to-maturity are classified as “available-for-sale securities”. Available-for-sale securities are recorded in the same way as trading securities; however, the mark-to-market adjustment is reported in stockholders’ equity under the caption “Unrealized gain from valuation of available-for-sale securities”, which are cancelled when the respective securities are sold, reporting the difference between net realizable value and acquisition cost within the results of operations.

It is necessary to evaluate whether at the consolidated balance sheet date there exists objective evidence of impairment, considering the difference between the initial carrying value of the security net of any principal payment or amortization and the fair value of the security. Any difference identified as impairment should be recognised in the income statement for the period.

Held-to-maturity securities-

Held-to-maturity securities are those securities that the Bank has the ability and intent to hold until maturity, and that have defined payments. Held-to-maturity securities are initially recorded at fair value and subsequently at amortized cost. Interest is recognized in income as earned. When securities mature, the difference between the actual amount received and the net book value is recognized in the consolidated statement of income within “Financial intermediation income”.

If objective evidence of impairment exists in respect of held to maturity securities, the value of the security should be reduced and the impairment amount should be recognised in the current year income consolidated statement.

Transfers between categories-

In the case of Bank the sale of securities to be held to maturity must be reported to the Banking Commission. Likewise, securities may be reclassified from the categories "trading securities" and "available-for-sale securities" to the category "held to maturity securities" or from “trading securities” to “available-for-sale securities”, as long as the Banking Commission grants its authorization. Also, they can be reclassified from the category "held to maturity securities" to "available-for-sale securities", provided that there is no intention or the capacity to keep them to maturity.

In the case of the insurance company only securities transfer from/to securities “held to maturity” and “available-for-sale” categories are permitted, provided that Investment Committee approval has been granted and that these transactions do not create gaps in the technical reserves coverage and minimum capital guarantee.

During 2014 and 2013, there were no transfers between categories.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

For operations where no settlement is agreed upon immediate or same day value date, on the date of the agreement the right and / or the obligation should be recorded in the clearing accounts until the liquidation is settled. In cases where the receivable is not settled within 90 calendar days from the date on which it was registered in clearing accounts, it will be reclassified as past due debt and estimation should be registered for the total amount.

(f) *Securities under repurchase/resell agreements-*

Repurchase agreements that do not comply with the terms set out in criterion C-1 “Recognition and derecognition of financial assets”, have been treated as collateralized financing transactions, reflecting the economic substance of such transactions and regardless of whether they are “cash based” or “securities based”.

The Group when recording these transactions as financing transactions recognizes the receipt of cash or an account receivable, as well as an account payable for the agreed price, which represents the obligation to repay that money, and reclassifies the financial asset as restricted collateral. When the Group is acting as the provider of finance, it recognizes the payment of cash or an account payable and also registers an account receivable in respect of the agreed price, which represents the right to recover the cash provided and recognizes the collateral received in a memorandum account. Over the life of the repo, the account payable or receivable are presented in the consolidated balance sheet as debtors or creditors as appropriate, and are valued at amortized cost, recognizing interest in the results for the year as it accrues, according to the effective interest method. The accrual of interest arising from the repo operation will be presented under the heading of “Interest income” or “Interest expense”, as appropriate.

In relation to the financial assets that have been sold or pledged as buyer of securities, there is recognition of an account payable for the obligation to restore the collateral to the seller, which is valued at fair value in the event of a sale and at the amortized cost if the assets were pledged in a repurchase transaction.

The differential, if any, that is generated by the sale of or using the security as collateral will be presented under the heading of “Financial intermediation income”.

In accordance with the dispositions of the Central Bank, any repurchase transaction, with a maturity period over three days must include an obligation to guarantee such transaction, when the fluctuations in the value of the securities under the repurchase agreement represents a net exposure which exceeds the maximum amount agreed by the parts.

The collaterals granted (without transfer of ownership) are recorded in the securities portfolio as securities for trading or in collateral, and if it corresponds to cash deposits, are registered under the cash and cash equivalents account as a restricted asset.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

Securities under repurchase/resell agreements that cannot be renegotiated with a third party are reported as secured borrowing or lending transactions. Premiums are recognized in income as they accrued, on a straight-line basis, throughout the term of the transaction.

(g) *Securities lending-*

In operations where the Group transfers securities to a borrower and receives other financial assets as collateral, it recognizes the fair value of the securities lent as restricted, while financial assets received as collateral (including cash managed in trusts), are recognized in memorandum accounts. When the Group receives securities in a securities lending transaction, it records the value of the securities in memorandum accounts while the financial assets provided as collateral are recognized as restricted (including cash managed in trusts). In both cases the financial assets received or delivered as collateral are recorded following the rules of valuation, presentation and disclosure in accordance with applicable accounting standard, while the values recorded in memorandum accounts are valued according to custody operation rules. The premium earned is recognized in the income statement, through the effective interest method over the life of the operation, against a receivable or payable as appropriate. The account payable which represents the obligation to repay the transaction value is reported in the consolidated balance sheet under the heading of “Collateral sold or pledged as guarantee”.

(h) *Derivative transactions-*

Transactions with derivative financial instruments comprise those carried out for trading or hedging purposes. These instruments are recognized at fair value, regardless of their classification.

(i) *Offsetting of clearing accounts-*

Amounts receivable or payable arising from investment securities, securities under repurchase/resell agreements, securities lending and/or derivative financial instruments which have expired but have not been settled at the consolidated balance sheet date as well as amounts receivable or payable resulting from the purchase or sale of foreign currencies which are not for immediate settlement or those with a same day value date, are recorded in clearing accounts included within “Other accounts receivable, net” and “Settlement transactions”.

The debit and credit balances of clearing accounts are offset as long as they have the contractual right to offset the amounts recorded at the same time, there is an intention to settle on a net basis or to realize the asset and settle the liability simultaneously.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

(j) *Past due loans and interest-*

Outstanding loan and interest balances are classified as past due according to the following criteria:

Commercial loans with principal and interest payable upon maturity – 30 calendar days or more after due date.

Commercial loans with principal payable upon maturity and periodic interest payments – When interest or principal have not been collected in 90 calendar days after their due date, respectively.

Commercial loans with principal and interest instalments –when principal and interest have a period of 90 calendar days or more past due.

Revolving credits, credit cards and others – when unpaid for two past due billing cycles or when the billing period is not monthly, at the equivalent of 60 calendar days or more of past due.

Mortgage loans - when the outstanding balance of a loan has unpaid instalments for 90 or more calendar days overdue.

Overdrafts from checking accounts without lines of credit – when the overdraft arises.

Additionally, a loan is classified as due when there is evidence that a debtor is declared in bankruptcy protection “concurso mercantil”, except for loans that continue being paid, which were granted for maintaining the entity’s ordinary operation and the liquidity required during the commercial insolvency proceedings as provided by section VIII of article 43 of the Commercial Insolvency and Bankruptcy Law “Ley de Concursos Mercantiles”, as well as the loans granted for maintaining the entity’s ordinary operation and the liquidity required during the commercial insolvency proceedings, provided that the trader continues managing its company and the bankruptcy reorganization referee has defined the guidelines whereby they were authorized, which payment priority shall follow the payment of loans owed to employees for salaries or wages accrued during the last year and severance payments, in accordance with the provisions of article 75, with regard to sections II and III of article 224 of said Law.

Non-current loans for which fully settled outstanding balances is made (including interest) and restructured or renewed loans showing sustained payment of credit, are reclassified as current. When those loans are reclassified to current portfolio, interest recorded in memorandum accounts, are recognized in consolidated statement of income at the moment of reclassification.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

(k) Restructured loans –

The Group has eligibility for credit restructuring, which generally consider that the terms of such restructuring are based on the repayment capacity of borrowers depending on each of the different types of credit.

Non-performing loans that are restructured or renewed remain within nonperforming loans, while there is no evidence of sustained payment.

Loans with a single payment of principal to maturity and periodic interest payments and credits with a single payment of principal and interest at maturity that are restructured during the term of the loan or renewed at any moment shall be considered as non-performing loans until there is evidence of sustained payment.

Those categorized as revolving credit, which are restructured or renewed at any time shall be deemed performing only when the borrower liquidated all of the accrued interest, the credit is not in arrears, and counts with elements indicating the ability to pay of the debtor.

Performing, loans other than those mentioned in the two preceding paragraphs, which are restructured or renewed shall be deemed to remain performing only if they meet the following:

- The life of the loan is bellow 80% of the original term of the loan, when the borrower has:
 - i) Covered all of the accrued interest, and
 - ii) Covered the principal of original loan amount, which at the time of the renewal or restructuring should have been covered.
- If the loan is restructured or renewed during the course of the final 20% of the original term of the loan, when the borrower has:
 - i) Paid all accrued interest
 - ii) Covered the entire original loan amount that at the date of the renewal or restructuring should have been covered and
 - iii) Also covered 60% of the original loan amount.

Should not all the conditions described above meet, then they are considered to be past due from the moment they are restructured or renewed, and until there is evidence of sustained payment.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

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(Millions of pesos)

When, as of the reorganization date, the loan payment is fulfilled for the total amount of the principal and interest payable, and only one or various of the following original loan conditions are modified: a) Collateral guaranties that imply the extension or replacement of collateral guaranties for better ones, b) Interest rate, when the interest rate agreed is improved, c) Currency, provided that interest rate corresponding to the new currency is applied, and d) Payment date, provided that such change does not imply to exceed or modify the payment periodicity or to allow any payment omission: for accounting purposes, the loan shall be maintained as current.

(I) Allowance for loan losses–

The allowance for loan losses, according to the administration, is sufficient to cover any losses that may arise from loans in its portfolio of loans and credit risk guarantees and irrevocable loan commitments. The allowance for loan losses is determined as follows:

Rated loans - The loan portfolio is classified according to the rules issued by the Ministry of Finance and Public Credit (SHCP for its acronym in spanish) based on the "General provisions applicable to credit institutions" (the "Regulations") issued by the Banking Commission, using the standard methodology for commercial loans, consumer and mortgage. The methodology distinguishes credit risk ratings and based on this determines the reserve.

On June 24, 2013, the Banking Commission published in the Federal Official Gazette a resolution whereby the Provisions are amended for the creation of preventive reserves for other commercial loans other of States, Municipalities and Investment Projects with own source of payment to adopt an expected loss, considering the probability of default, the loss given default and the exposure at default. In addition, the commercial loan portfolio is classified in two groups: the first group includes those with annual sales fewer than 14 million UDIS, where quantitative factors are assessed and the second group includes borrowers with annual sales equal to or greater than 14 million UDIS, which are also assessed for qualitative factors.

The resolution came into force on the following day of its publication and it was resolved that the application of the new criteria concerning the commercial loan portfolio would occur by December 31, 2013, allowing early application and the recognition of the financial effects from the application of the new methodology in stockholders' equity of the institutions.

On June 30, 2013, and in accordance with the provisions of transitory article two, the Group adopted the new methodology, recording a charge in stockholders' equity of \$799 (\$559 net of deferred tax) for the year ended on December 31, 2013, with regard to the creation of allowance loan for losses for loans granted to financial entities, the new methodology was applied since March 2014 in accordance with the transitory article three, set forth the mandatory recognition of the financial impact for the creation of allowances not later than June 30, 2014. As a result, the Group recognized a charge in stockholders' equity of \$30 (\$21 net of deferred tax) (note 4(a)).

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

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(Millions of pesos)

On October 30, 2014, the Banking Commission published in the Official Gazette a resolution whereby the Provisions relating to the methodology for rating allowance for loan losses for expected credit risk loss, were amended. This amendment is aimed to make the methodology consistent with the amendment to the Commercial Insolvency and Bankruptcy Law published on January 10, 2014 in the Official Gazette, whereby section II of article 339 of the Commercial Insolvency and Bankruptcy Law was amended in order to set forth that the request for acceptance of commercial insolvency with a preliminary reorganization plan shall be undersigned by the client with the holders of at least the simple majority of the total debtors: the amended methodology provides that the reserves may be calculated by applying the calculation provided by article 114 of the Provisions, based on the following:

- I. For the portion hedged with collateral guaranties, the estimate is not modified and is applicable in the same way than to the rest of the clients subject to rating.
- II. For the unhedged portion of the loan, “best estimate of expected loss” shall be made, considering the client’s default and the expected payments and/or loss mitigating factors that may be proved by the client.

In compliance with the foregoing paragraphs, the Bank estimated as “best estimate of expected loss” 45% (Loss Severity) for those clients declared in bankruptcy protection. This amended methodology was applied from the effective date, pursuant to the Provisions.

The current methodology published in the Federal Official Gazette on October 5, 2011 that is based on concepts such as: expected loss, probability of default, exposure at default and loss given default by loan and borrower applies for States, Municipalities and Investment Projects; considering mainly the ratings provided by rating agencies.

For Investment Projects with own source of payment, an individual evaluation is conducted, considering the Construction and Operation stages.

The allowance for loan losses is determined depending on the risk level as shown on the next page.

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GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

Risk level	Range of percentage of allowance for loan losses				
	Consumer loans		Residential		Commercial
	<u>Non revolving</u>	<u>Revolving</u>	<u>Mortgage</u>		
A – 1	0.00 – 2.00	0.00 – 3.00	0.00 – 0.50	0.00 – 0.90	
A – 2	2.01 – 3.00	3.01 – 5.00	0.501 – 0.75	0.901 – 1.50	
B – 1	3.01 – 4.00	5.01 – 6.50	0.751 – 1.00	1.501 – 2.00	
B – 2	4.01 – 5.00	6.51 – 8.00	1.001 – 1.50	2.001 – 2.50	
B – 3	5.01 – 6.00	8.01 – 0.00	1.501 – 2.00	2.501 – 5.00	
C – 1	6.01 – 8.00	10.01 – 5.00	2.001 – 5.00	5.001 – 10.00	
C – 2	8.01 – 15.00	15.01 – 35.00	5.001 – 10.00	10.001 – 15.50	
D	15.01 – 35.00	35.01 – 75.00	10.001 – 40.00	15.501 – 45.00	
E	35.01 – 100.00	75.01 – 100.00	40.001 – 100.00	45.001 – 100.00	

The Dispositions establish rules for the creation of allowances that recognize potential losses in the loan portfolio and of foreclosed assets or received in lieu of payment over time.

General reserves – in accordance with the Dispositions risk grade A and B-1 from the revolving consumer portfolio are considered general reserves.

Specific reserves – those reserves resulting from loans with risk grade B, C, D and E, but not including those which result from risk grade B-1 from the revolving consumer portfolio.

Exempt portfolio – consists mainly of loans to the Bank Savings Protection Institute (IPAB for its acronym in Spanish), which are not rated.

Impaired loans – commercial loans which are not likely to be fully recovered. Both, current and past due portfolios may be identified as impaired loans. For consolidated financial statement disclosure purposes, “impaired loans” are those commercial loans classified by the Group as having the risk levels “D” and “E”.

Additional reserves – are those that are created for hedging risks that are not provided by the various methodologies for rating the loan portfolio. Also included are estimates for items such as uncollected ordinary interest accrued and other ancillary charges, as well as reserves required by the Banking Commission.

Loans considered irrecoverable are written off against the allowance when their collection is determined to be impractical. Recoveries derived from loans written off are recognized in income of the year.

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GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES**Notes to Consolidated Financial Statements**

(Millions of pesos)

As a result of the rating process, increases or decreases in the preventive loan loss reserve are recorded in the year's income (loss), adjusting the financial margin.

When the balance of the preventive loan loss reserve exceeds the amount required in accordance with the rating methodologies, the difference is cancelled on the date on which the next rating for type of loan (commercial, consumer or housing) versus the year's income (loss) occurs, affecting the preventive loan loss reserve. In cases where the amount to be cancelled exceeds the recorded balance of such allowance in the year's income (loss), the excess is recognized in "Other operating income".

Claim reductions, debt cancellations, rebates and discounts are recorded as charges to the preventive loan loss reserve. If the amount of the latter exceeds the balance of the reserve associated with the loan, reserves for up to the amount of the difference are created in advance.

(m) Premium debtors-

Uncollected premiums represent under 45-days aging balances in accordance with the Insurance and Bonding Commission's provisions; which when older must be written off against the results of operations for the year.

Management conducts an assessment to estimate the recoverable amount of accounts receivable from identified debtors whose maturity is agreed at inception over a period greater than 90 calendar days if necessary an allowance for doubtful accounts is created.

In the case of accounts receivable not included in the last paragraph of previous page, the estimate for allowance for doubtful accounts is made for the full amount of the debt in accordance with the following periods: within 60 calendar days of initial registration, debtors when they relate to unidentified debtors and 90 calendar days of initial registration if they relate to debtors identified.

(n) Other accounts receivable-

Loans to officers and employees, collection rights (when they do not represent impaired loans), and other receivables from identified debtors, whose agreed-upon maturity does not exceed 90 calendar days, are assessed by management to determine their estimated recovery value and, where applicable, a loan loss reserve is created. Amounts receivable from other accounts receivable, that are not recovered within 90 days subsequent to their initial recording (60 days if balances are unidentified) are totally reserved, except for those related to recoverable tax balances, value added tax, and clearing accounts. This caption also includes debtors on settlement of 24 and 48-hour foreign currency sales transactions.

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GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

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(o) Foreclosed assets-

Foreclosed assets are recorded at the lesser of: (a) cost, (b) its fair value deducted from the strictly necessary costs and expenses that are incurred in the adjudication and (c) the value of the asset or amortizations due or overdue that led to the adjudication, net of its estimates.

When the book value exceeds the value of the foreclosed asset, the difference will be recognized in the consolidated statement of income of the year as part of "Other operating income". In the case of a promise of sale-and-repurchase agreements including ownership reserves, these transactions do not comply with the requirements of accounting criteria C-1 "Recognition and derecognition of financial assets". In this case the asset should be recognized and classified as restricted, depending on the relevant type of asset, at the book value on the date of the agreement, even if the agreed sale price is higher than the book value.

Payments received in advance in relation to the aforementioned assets are recorded as a liability. The gains or losses arising from these transactions are recorded in "Other operating income" on the date that the conditions to consider that the ownership has been transferred in accordance with accounting criteria C-1 are met.

The Group creates additional reserves on a quarterly basis to recognize potential losses for the impairments in asset value due to the passing of time. These reserves are created in accordance with the Dispositions which are determined as follows:

Elapsed months since the date of foreclosure or lieu of payment		<u>Percentage of the allowance</u>	
		<u>Real Estate</u>	<u>Goods receivables and security investments</u>
More than:	6	0	10
	12	10	20
	18	10	45
	24	15	60
	30	25	100
	36	30	100
	42	35	100
	48	40	100
	54	50	100
	60	100	100

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GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

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(Millions of pesos)

In any cases, the reserve percentage is applied to the foreclosure value obtained from the applicable accounting standards. Regarding valuations after the foreclosure, which result in the reduction of the foreclosed assets, the percentages of preventive reserves are applied on such adjusted value.

(p) *Property, furniture and equipment-*

Property, furniture and equipment are initially recorded at acquisition cost and through to December 31, 2007, for being the last year considered as inflationary economic environment under FRS “B-10” were adjusted for inflation by using factors derived from the UDI.

Depreciation and amortization are calculated using the straight – line – method over the estimated useful life of the assets. The useful life of the principal assets classes are show on note 16.

(q) *Permanent investments in shares-*

Investments in affiliated and associated companies are valued using the equity method, which recognizes changes in income (loss) of the year. It is also included under this caption other permanent investments in which there are no significant influence, which are recorded at their acquisition cost.

(r) *Goodwill-*

Goodwill represents the future economic benefits that arise from other assets acquired that are not individually identifiable or separately recognized. Goodwill is subject to impairment tests at least annually.

(s) *Other assets, deferred charges and intangibles-*

Other assets include recoverable balances of taxes pending to be offset or recovered. Deferred charges include the prepayment of labour obligations and other expenses pending amortization arising from services and commissions paid in advance, whose amortization is made on straight line over the term of the related transaction.

“Intangible Assets” includes costs directly related to the installation and commissioning of software and the cost of the necessary licenses to operate such equipment. According to the internal policies of the Group, only projects that comply with the following characteristics are subject to be capitalized: (i) the assets are identifiable, (ii) the Bank has control over the assets and (iii) that there will be anticipated future economic benefits from them. The average life of these assets which are amortized on a straight line basis is 3 to 5 years, based on its characteristics.

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GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

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(Millions of pesos)

(t) *Income tax (IT) and employee statutory profit sharing (ESPS)-*

IT and ESPS payable for the year are determined in conformity with tax regulations in force at December 31, 2014 and 2013.

Deferred IT and deferred ESPS are accounted for under the asset and liability method which compares accounting and tax values. Deferred income tax and ESPS (assets and liabilities) are recognized for the future tax consequences attributable to temporary differences between the consolidated financial statement carrying amounts of existing assets and liabilities and their respective tax bases, in the case of income tax for unamortized tax losses carry forward and unused tax credits.

Deferred assets and liabilities for income tax and ESPS are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities and ESPS of a change in tax rates is recognized in results of operations for the period the change is enacted.

(u) *Deposit funding-*

This caption includes money market demand and term deposits made by the general public including debt securities issued. Interest is recognized in operations on the accrual basis. Regarding those instruments placed at a price other than par value, difference between the instrument par value and the cash amount received for it, is recognized as a deferred charge for issue expenses, under the caption "Other assets, deferred or intangible charges", or a deferred credit in the liability that gave rise to it in the case of a premium or discount for placement and is amortized under the straight-line method against interest expense or interest income during the term of the instrument that generated it.

(v) *Due to banks and other institutions-*

Bank and other loans comprises short and long-term bank loans, as well as loans obtained through credit auctions with Central Bank and development fund financing. In addition, this category includes loans rediscounted with agencies specializing in financing economic, productive or development activities. Interest is recognized on accrual basis. In the case of interbank loans received within less or equal to 3 days are presented as part of the category of immediate enforceability.

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GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

(w) *Technical reserves-*

The creation and increases of technical reserves are made in accordance with the terms and in the percentages established in the LGISMS. The valuation of these reserves is reported, as required by the Insurance and Bonding Commission, by an independent actuarial auditor registered with the Insurance and Bonding Commission itself. The Group used methods for the valuation of technical reserves in compliance with the provisions established by the Insurance and Bonding Commission, such methods are registered with the Insurance and Bonding Commission. Following are the most significant aspects for the determination and accounting for aforementioned reserves:

Current risk reserve-

Pursuant to the provisions of Chapter 7 of the Insurance Regulation Letter (Circular Única de Seguros) insurance institutions register on the Insurance and Bonding Commission the technical notes and the actuarial methods used for creating and valuing the current risk reserve.

The current risk reserve for life insurance with terms of up to one year, and insurance covering accidents, health and property and casualty includes the excess of the projection of future claims obligations over the amount of unearned premiums and administrative expenses.

The valuation of this reserve is conducted on a monthly basis, whereas the adequacy of this reserve is evaluated on a quarterly basis and allows for assigning resources in advance to likely obligations from claims that exceed the amount of unearned premiums.

For purposes of calculating the adequacy index of the current risk reserve, the casualty or accident rate information for casualty insurance was based on the last 5 years.

Life insurance with terms in excess of one year - This reserve may not be less than the reserve obtained by applying the actuarial method for determining the minimum current risk reserve amount that the Insurance and Bonding Commission establishes to such end through rules of a general nature.

The balance of this reserve is evaluated on a quarterly basis and allows for assigning resources in advance to the likely obligations from claims that exceed the amount of unearned premiums. Formerly, resources were only assigned at the time the claim was filed.

Mathematical pension reserve – the current risk reserve or mathematical pension reserve corresponds to the amount which, capitalized at the technical interest rate, guarantees the payment of future rents according to the demographic tables adopted.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

Reserve for claims and maturities-

This reserve has the following components:

- The obligation under specific known claims that were recorded by the Group but not yet paid at the year end. Its increase occurs in accordance with the claim of insured events occurred, in life products for the face amount and based on the estimations done by the Group of the amount of the obligation by the covered risks in accident and health and property and casualty operations. In case of reinsurance ceded, simultaneously a corresponding recovery is recorded.

Auto insurance claims are shared with coinsurers equally 50% on the basis of casualty or accident rate information provided the latter.

- Reserve of claims pending of valuation. This calculation is done applying the actuarial methodology developed by the Group and authorized by the Insurance and Bonding Commission. This reserve corresponds to the expected value of future claim payments that being reported during the current year or in prior years, may be paid in the future and the exact value is not known. This methodology considers the average claim amount paid in prior years for each one of the insurance lines, based on actual payment experience and the average estimated amount for future payments of the same kind of claims.

Reserve for claims incurred, but not reported-

Pursuant to the rules established by the Insurance and Bonding Commission, the Group is required to set up this reserve for recognizing the estimated amount of events that have occurred but that the insured has not reported to the Group, which includes an estimate of the relevant adjustment in expenses. This estimate is made based on the own experience concerning events, in accordance with the methodology proposed by the Group's specialists and approved by the Insurance and Bonding Commission.

That methodology establishes that the calculation of the reserve for incurred but not reported events takes into consideration two effects: the first one relates to the time the insured takes for reporting the event to the Group, and the second one relates to the time it takes for the Group to estimate and adjust the amount of the loss, in accordance with its estimation and recoding practices. To segregate these effects, the registered method recognizes two components: reserve for incurred but not reported events (SONOR for its initials in Spanish) and reserve for reported but not yet paid events (SORNOF for its initials in Spanish).

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

The SORNOF is computed based on the gross incidence of events, affected by a factor that considers pending unrecorded adjustments through payment of the events already reported. The retained amount is computed based on the information on retained events of each policy.

Furthermore, the reserve for incurred but not reported events is determined as the global reserve computed based on the technical notes registered for each operation, less the SORNOF amount obtained.

Reserve for policy dividends-

This reserve is determined based on an actuarial estimation, considering gains from individual life, group life, personal accidents and miscellaneous others.

Contractual obligations reserve-

This reserve includes annuities paid to pensioners or beneficiaries, which period has expired without such annuities being claimed and there is no evidence that the beneficiaries are no longer eligible or have died.

Contingency reserve-

The resources of this reserve are intended to confront an adverse deviation in obligations derived from the demographic hypotheses used for the determination of the amounts required for taking out annuity insurance with an insurance company (annuity amount), which would translate into excessive obligations as a result of a variation in the mortality rate used in the demographic table adopted.

Special reserves (reserve for investment fluctuations)-

The purpose of these reserves is to support insurance companies against potential variations in the returns on their investments. The reserve will be created by using a portion of the financial return, which is the difference between actual returns on the institutions' investments and the minimum returns associated with their technical reserves.

(x) *Employee benefits-*

Termination benefits other than restructuring and retirement to which employees are entitled are recorded in the consolidated statement of income, based on actuarial computations using the projected unit credit method, considering the projected salaries. At December 31, 2014 and for purposes of recognizing benefits upon retirements, the remaining average service life of employees entitled to pension are approximately 13 years, for the seniority premium are 18 years and for other postretirement benefits are approximately 13 years (for 2013 16 years, 17 years and 13 years respectively).

(Continued)

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(Millions of pesos)

Actuarial gains or losses are recognized in the consolidated statement of income as accrued considering the remaining service life of the employees expected to receive plan benefits and are amortized based on life expectations of the group of retirees. In the case of pension plan of defined contribution and other defined contribution benefits are recognized in the statement of operations as accrued.

(y) *Share-based payment-*

The Group offers different payment program based on shares of its ultimate holding Company's equity for certain employees, recognizing an operating expense in the consolidated statement of income and a liability, during the vesting period, at fair value of the equity securities at the valuation date. The vesting period of the grant of such programs varies between one and three years.

Additionally, from October 2014, a voluntary savings scheme was implemented for purchasing shares of HSBC Holdings PLC (HGHQ) whereby for every three shares purchased by the employee, the Bank shall pay an additional share; for this purpose, the employee is required to comply with a three-year foreclosure period.

(z) *Revenue recognition-*

Interest on loans granted is recorded in income as earned. Interest on past due loans is not recognized in income until collected.

Fees and interest collected in advance are recorded as deferred income under "Deferred credits", and recognized in results of operations as earned.

The annuity and renewal fees for credit cards are deferred over a period of twelve months.

Fees charged for initially granting loans (personal, residential mortgages, and commercial loans) are recorded as a deferred credit, which is amortized against income of the year as interest income, pursuant to the straight-line method during the life of the loan. All other fees are recognized at the time they are generated in the line item of "fees and rates charged" in the consolidated statement of income. Costs and expenses associated with credit loans are recognized as deferred charge and amortized over the same period in which revenue is recognized by fees charged for granting of such credits.

The interest from repurchase transactions and securities lending are recognized as earned. Fees earned in connection with fiduciary operations and those arising from asset custody and management services are recognized in income as earned.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

(aa) Revenue recognition from insurance and reinsurance premium revenues-

Life – Revenue in this operation are recorded according to the issuing of receipts for payment, added premiums for reinsurance taken and reduced by reinsurance premiums ceded.

Accident and health and property and casualty – Income from these transactions is recorded based on the written premiums, added the reinsurance premiums taken, which are reduced by reinsurance premiums ceded.

The insurance premiums that the policy holder insured have not paid within the term provided by the LGISMS are automatically cancelled, thus releasing the current risk reserve and, in the case of reinstatement, the reserve is restored from the month in which the policy is renewed.

Pensions – the annuity amount calculated on the date the Mexican Social Security Institute issues the document for granting the pension is considered the insurance premium, which is recorded at the time the policy is issued.

Salvage revenues - For accounting purposes, salvage revenues are recognized as an asset and a decrease in the cost of claims when determined, and are recorded at estimated realizable value.

Policy rights and premium surcharges - Revenues related to policy rights correspond to the recovery of costs of issuing the policy and are recognized on income statement at the time the policy is issued.

Revenue from surcharges on premiums corresponds to related financing policies with payments and are recognized in income as earned.

Net acquisition cost – the acquisition cost is recognized in the consolidated statement of income when the policies are issued, decreasing of reinsurance ceded fees.

(bb) Foreign currency transactions-

The accounting records are maintained in both pesos and foreign currencies, which for presentation of the consolidated financial statement purposes, in the case of currencies other than the dollar are translated from the respective currency into dollars as established by the Banking Commission and the dollar equivalence with Mexican currency is translated at the exchange rate established by the Central Bank. Foreign exchange gains and losses are recognized in the consolidated statement of income during the year.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

(cc) Contributions to the Institute for the Protection of Bank Savings (IPAB for its acronym in Spanish)-

Among other provisions, the Bank Savings Protection Law provides for the creation of the IPAB, is a system for protecting the bank savings of depositors and regulates the financial support granted to the commercial banking institutions to achieve this objective. The IPAB guarantees a maximum of 400,000 UDIS (\$2 at December 31, 2014 and 2013) by saver and by institution. The Bank recognizes in results of operations the mandatory contributions to the IPAB.

(dd) Contingencies-

Liabilities for loss contingencies are recorded when it is probable that a liability has been incurred and the amount of the assessment and/or remediation can be reasonably estimated. When a reasonable estimation cannot be made, qualitative disclosure is provided in the notes to the consolidated financial statements. Contingent revenues, earnings and assets are not recognized until their realization is virtually assured.

(ee) Impairment of recovery from long term assets-

The Group evaluates periodically the long term assets to determine whether there is an indication of potential impairment. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future net revenues expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated net revenues, an impairment charge is recognized by the amount by which the carrying amount of the asset exceeds the fair value of the asset. Assets to be disposed of would be separately presented in the consolidated balance sheets and reported at the lower of the carrying amount or realizable value.

(4) Accounting changes and reclassifications-***Accounting changes-***

- a) On June 24, 2013, certain amendments to the Provisions, relating to the methodology for rating the commercial loan portfolio granted to financial entities, were published in the Federal Official Gazette (DOF); individuals with business activities and legal entities other than: projects with own source of financing, as well as credit schemes commonly known as “structured”. The Group applied the new methodology for rating the commercial loan portfolio on March 2014, recognizing a charge to stockholders’ equity of \$30 (\$21 net of deferred taxes), in accordance with the transitory articles of such Provisions.

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GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

The preventive commercial loan loss reserve granted to financial entities, determined according to the new methodology applied from of March 2014 amounted to \$174, compared with that determined according to the methodology in effect prior to such date, which amounted to \$144.

The Bank did not determine the retrospective financial effect of the application of the methodology for loans granted to financial entities corresponding to the end of December 2013, in accordance with the provisions of official letter No. 113-1/17501/2015 submitted by the Banking Commission on January 8, 2015, whereby it provides that credit institutions may refrain from making comparative adjustments for the preparation of annual financial statements for periods preceding 2013, when it is impractical to determine the amounts corresponding to such periods due to the retrospective recognition of the application of new methodologies for rating the commercial loan portfolio, based on the expected loss and as set forth by the Provisions, and declaring although Management made all the reasonable efforts, it was not possible to obtain the historical information required by the new methodology. As a consequence, these consolidated financial statements do not include the information required in paragraph 11 of the FRS B-1 "Accounting changes and error corrections" by the Banking Commission in transitory article four of the amendments to the Provisions published on June 24, 2013.

- b) As mentioned in note 3(l), on September 24, 2014, the Ministry of Finance and Public Credit published in the Official Gazette a resolution whereby accounting standard B-6 "Loan Portfolio" of the Provisions is modified, providing that loans granted by credit institutions in accordance with article 75, with respect to sections II and III of article 224 of the Commercial Insolvency and Bankruptcy Law, and with regard to those loans that continue being paid in accordance with section VIII of article 43 of such Law, shall be considered as current portfolio, provided that these do not comply with the criteria set forth in the same standard for such loans to be considered past due. The foregoing is aimed at making loans consistent with the current methodology of loan reserves.
- c) The Mexican Board of Financial Reporting Standards (*Consejo Mexicano de Normas de Información Financiera, A. C.* or CINIF) issued the FRS C-11, C-12 and improvements to FRS that had no significant effects on the Bank's consolidated financial statement, either by not being applicable or absence of specific criteria issued by the Banking Commission, are shown below:
 - **FRS C-12 "Financial instruments with characteristics of liabilities and equity"** - FRS C-12 is effective for years beginning January 1, 2014.
 - **FRS C-14 "Transfer and retirement of financial assets"**- FRS C-14 is effective for years beginning on or after January 1, 2014.

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GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

2014 FRS improvements-

In December 2013, the CINIF issued the document referred to as “2014 FRS Improvements”, which contains precise modifications to some FRS. The modifications that bring about accounting changes effective starting on January 1, 2014, that did not have a material effect on the Group’s consolidated financial statements, are listed below:

- **FRS C-5 “Prepayments”-** FRS C-5 provides that amounts paid in foreign currency must be recognized at the exchange rate in force as of the transaction date, and shall not be modified as a result of foreign exchange fluctuations between the functional currency and the foreign currency in which the prices of goods and services regarding such prepayments are denominated. Additionally, it provides that impairment losses arising from prepayments, as well as the reversal of such losses, shall be reported as part of the net income or loss for the period.
- **Bulletin C-15 “Impairment or disposal of long-lived assets”-** Bulletin C-15 provides that the impairment loss for a long-lived asset in use, as well as the reversal thereof, and the impairment loss of long-lived available-for-sale assets, including increases or decreases, shall be reported in the results of operations for the period, under the same financial statement captions to costs and expenses, where depreciation and amortization are recognized. Impairment losses and reversal thereof, for indefinite-lived intangible assets, including goodwill, shall be presented in the results of operations for the period, under the financial statement caption associated with depreciation and amortization expense on assets of the cash generating unit to which these intangible assets relate. Under no circumstances shall impairment losses be included as part of the costs that have been capitalized in the carrying value of an asset.

Likewise, it sets out that for purposes of reporting the impairment losses of associates, joint ventures and other investments, and the goodwill thereof, the provisions of FRS C-7 shall be complied with. FRS C-7 provides that impairment losses be recognized under the financial statement caption associated with equity in earnings or loss of investees.

Additionally, Bulletin C-15 sets out that assets and liabilities identified with discontinued operations shall be presented in the statement of financial position, grouped in a single financial statement caption within assets and a single financial statement caption within liabilities, classified as short-term, and shall not be presented on a net basis. However, these items shall be reported as long-term in the event of sale agreements that are essentially purchase options and sale - leaseback agreements. It also provides that the entity shall not restate previously issued statements of financial position as a result of such reclassification.

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GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos, except otherwise indicated)

Reclassifications-

As mentioned in note (31(a)), certain accounts of the financial margin for the year ended December 31, 2013, were reclassified to make them comparable to the presentation used as of December 31, 2014, with the objective to identify revenue and expenses related to hedging operations. Such reclassification did not affect financial margin.

(5) Foreign currency exposure-

Central Bank regulations require that banks and brokerage firms maintain balanced positions in foreign currencies within certain limits. The short or long position permitted by the Central Bank is equal to a maximum of 15% of the Bank's basic capital and 15% of the Brokerage firm's net capital. In accordance to the basic capital of the Bank, as published by the Central Bank as of December 31, 2014 and September 30, 2013, the maximum exposure permitted as of December 31, 2014 and 2013, amounts to USD\$423 million and USD\$491 million, respectively.

The foreign currency position as of December 31, 2014 and 2013 is analyzed as follows:

	<u>(Millions of dollars)</u>	
	<u>2014</u>	<u>2013</u>
Assets	40,541	38,064
Liabilities	<u>(40,262)</u>	<u>(37,935)</u>
Net assets (liabilities)	279	129
	=====	=====

The exchange rate of the peso to the dollar as of December 31, 2014 and 2013 was \$14.7414 and \$13.0843, respectively. The exchange rate on February 11, 2015, the date of issuance of the consolidated financial statements was \$15.1099 pesos per dollar.

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GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

(6) Cash and cash equivalents-

At December 31, 2014 and 2013, cash and cash equivalents are analyzed as follows:

		<u>2014</u>	<u>2013</u>
Cash	\$	13,901	12,251
Deposits with domestic and foreign banks		6,942	6,965
Other cash equivalents		1	1
Restricted cash and cash equivalents:			
Central Bank deposits		21,233	32,599
Bank loans with maturity up to three days		160	2,988
24 and 48-hour foreign currency purchases		9,555	40,729
24 and 48-hour foreign currency sales		<u>(11,102)</u>	<u>(40,126)</u>
	\$	40,690	55,407
		=====	=====

At December 31, 2014 and 2013, cash balances valued in Mexican pesos by currency included in the cash and equivalents caption is as follows:

<u>Currency</u>	<u>Exchange rate</u>			<u>2014</u>	<u>2013</u>
	<u>2014</u>	<u>2013</u>			
Mexican peso	\$	-	\$	13,671	12,104
Dollar	14.7414	13.0843		229	146
Euro	17.8386	18.0302		<u>1</u>	<u>1</u>
			\$	13,901	12,251
				=====	=====

At December 31, 2014 and 2013, the Group did have deposits in dollars with the Central Bank for \$10 and \$6, respectively.

On June 9, 2014, circulars 9/2014 and 10/2014 issued by the Central Bank, were published in the Official Gazette. These set forth that the monetary regulation deposit may comprise cash or securities, or both, in the proportions determined by the Central Bank, and securities in which such deposit may be invested shall be limited to the Monetary Regulation Bonds of Limited Negotiability (BREMS-L, see note 8). Based on this regulation, the Bank modified the composition of its monetary regulation deposit and now is composed by a cash portion and a securities portion. In addition, based on circular 11/2014 issued by the Central Bank, the amount required as monetary regulation deposit shall be \$3,085.

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GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

At December 31, 2013, the deposits with the Central Bank in local currency relates to monetary regulation deposits with no specific term and bear interest at the average rate of deposit fundings.

At December 31, 2014 and 2013 the Group has call money loans with 3-day maturities (did not have call money at December 31, 2012) analyzed as follows:

	2014		2013	
	<u>Rate</u>	<u>Amount</u>	<u>Rate</u>	<u>Amount</u>
Cash	3.00%	\$ 21,221	3.60%	\$ 32,405

At December 31, 2014 and 2013, the Group has call money loans with 3-day maturities, shown as follows:

Counterparty	2014			2013		
	<u>Days</u>	<u>Rate</u>	<u>Amount</u>	<u>Days</u>	<u>Rate</u>	<u>Amount</u>
Nacional Financiera, S. N. C.	2	3%	\$ 160	2	3.50%	\$ 1,600
Banco Mercantil del Norte, S. A.	-	-	-	2	3.45%	650
Banco Nacional de México, S. A.	-	-	-	2	3.40%	738
			\$ 160			\$ 2,988
			===			=====

At December 31, 2014 and 2013 currencies receivable and deliverable on purchases and sales to be settled in 24 and 48 hours, translated into pesos, are analyzed as follows:

Currency	2014		2013	
	<u>Purchased</u>	<u>Sold</u>	<u>Purchased</u>	<u>Sold</u>
Dollar	\$ 7,247	(8,849)	30,061	(29,544)
Sterling	-	-	-	(49)
Euro	79	(39)	117	(3)
Brazilian real	2,203	(2,203)	10,368	(10,452)
Other currencies	26	(11)	183	(78)
	\$ 9,555	(11,102)	40,729	(40,126)
	=====	=====	=====	=====

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

(7) Margin accounts-

On December 31, 2014, the margin accounts relate to deposits at the Mercado Mexicano de Derivados, S. A. de C. V. (MexDer) amounting to \$7.

(8) Investment securities-

At December 31, 2014 and 2013 the investments in securities are analysed as follows:

	<u>2014</u>		<u>2013</u>	
<u>Trading*:</u>				
Government securities	\$ 47,874		49,353	
Banking promissory notes	1,105		2,240	
Bonds	1,840		1,656	
Equities	<u>4,185</u>	55,004	<u>5,319</u>	58,568
<u>Available-for-sale*:</u>				
Government securities	128,323		92,117	
Bank securities	518		508	
Corporate securities	<u>3,686</u>	132,527	<u>3,456</u>	96,081
<u>Held-to-maturity*:</u>				
Special CETES of the				
UDIS Trusts:				
Mortgages	-		4,323	
States and municipalities	5,103		627	
BREMS L**	14,302		-	
Corporate securities	1,225		1,303	
Government securities	11,000		10,215	
Bonds	223		210	
Bank securities	<u>149</u>	<u>32,002</u>	<u>95</u>	<u>16,773</u>
Total investment securities	\$ 219,533		171,422	
	=====		=====	

* The total of trading and available-for-sale securities which have been pledged as collateral, as explained later in the collateral section.

** Based on the regulation issued by the Central Bank (see note 6), the Group modified the composition of the monetary regulation deposit and included a securities portion represented by Monetary Regulation Bonds (BREMS L). During 2014 and 2013, the Group did not record any transfers between categories of investment securities.

During 2014 and 2013, the Group did not record any transfers between categories of investment securities.

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GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

Collaterals

At December 31, 2014 and 2013 securities pledged and received as collateral, including collateral sold or pledged as a guarantee were as follows:

	<u>2014</u>	<u>2013</u>
<i><u>Pledged (Restricted securities) (note 9)</u></i>		
Trading securities	\$ 33,319	28,292
Securities available for sale	35,420	16,922
Held to maturity	<u>14,302</u>	<u>-</u>
	\$ 83,041	45,214
	=====	=====
<i><u>Received (in memorandum accounts) (notes 9 and 10)</u></i>		
In respect of repo transactions	\$ -	8,008
In respect of securities loan:		
Fixed income	<u>21,979</u>	<u>9,283</u>
	\$ 21,979	17,291
	=====	=====
<i><u>Collateral sold or pledged as guarantee</u></i>		
In respect of repo transactions (note 9)	\$ -	7,507
In respect of securities loan:	11	-
Fixed income	<u>21,886</u>	<u>9,076</u>
	\$ 21,897	16,583
	=====	=====

Collateral pledged, received or sold and given as a guarantee, originated primarily from repo transactions and stock borrowing and lending transactions. Collaterals received are recorded in memorandum accounts whilst the collaterals sold or pledged as guarantees are recorded in the account "Collateral sold or given as guarantee" whose balance in the case of repo transactions is presented net of the collaterals received in the consolidated financial statements.

At December 31, 2014 and 2013, the Group had the right to pledge as a guarantee, the collateral received in sale and repurchase transactions or the right to sell or pledge the collateral received in stock borrowing transactions.

At December 31, 2014 and 2013 the Group maintains, investments (other than government securities), from the same issuer exceeding 5% of the Bank's net capital (As of December 31, 2014 and September 30, 2013 of \$2,542 and \$2,649, respectively), for a total value of \$6,724 and \$15,153, respectively, as shown in the following page.

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Notes to Consolidated Financial Statements

(Millions of pesos)

<u>Issuer</u>	<u>Symbol</u>	<u>Series</u>	<u>Amount</u>	<u>Rate</u>
<u>2014</u>				
Brazilian government	LTN6Y1	150701	\$ 2,652	12.38%
Brazilian government	LTN731	151001	<u>4,072</u>	12.40%
			\$ 6,724	
			=====	
<u>2013</u>				
Brazilian government	BNTN071	140101	\$ 4,200	4.83%
Brazilian government	BLTN6M6	140101	6,254	9.49%
Brazilian government	BLTN6Z8	140101	<u>4,699</u>	10.36%
			\$ 15,153	
			=====	

Classification of investment securities -

At December 31, 2014 and 2013, the classification of investment securities in accordance to their nominal term of the securities portfolio in short and long term, is as follows:

<u>Securities</u>	<u>2014</u>		<u>2013</u>	
	<u>Short term</u>	<u>Long term</u>	<u>Short term</u>	<u>Long term</u>
Trading	\$ 24,097	30,907	38,239	20,329
Available-for-sale	227	132,300	11,248	84,833
Held-to-maturity	877	31,125	<u>640</u>	<u>16,133</u>
	<u>25,201</u>	<u>194,332</u>	<u>50,127</u>	<u>121,295</u>
	\$ 219,533		171,422	
	=====		=====	

The weighted averages of maturity terms in years (unaudited), of investments in securities classified by categories at December 31, 2014 and 2013 is shown below:

<u>Securities</u>	<u>2014</u>	<u>2013</u>
Trading	2.38	1.68
Available-for-sale	2.54	2.79
Held-to-maturity	9.48	10.50

(Continued)

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The weighted average rates (unaudited) and interest income from securities at December 31, 2014 and 2013 (refer to note 31), is shown below:

<u>Securities</u>	<u>2014</u>		<u>2013</u>	
	<u>Interest</u>	<u>Rate</u>	<u>Interest</u>	<u>Rate</u>
Trading	\$ 2,102	2.42%	\$ 1,467	3.26%
Available-for-sale	5,415	4.15%	4,467	4.97%
Held-to-maturity	<u>1,093</u>	4.48%	<u>826</u>	5.27%
	\$ 8,610		\$ 6,760	
	=====		=====	

During the years ended December 31, 2014 and 2013, the net losses and gains in respect of available for sale securities were \$164 and \$43, respectively.

During the years ended December 31, 2014 and 2013, the Group did not record any losses caused by impairment in available for sale or held to maturity securities.

The gain derived from the valuation of available for sale securities recognised in the stockholders' equity at December 31, 2014 and 2013 were \$877 and \$23, respectively, and the Group reclassified to the statement of income \$513 and \$883, respectively, on the sale of various available for sale securities. Due to the above the net effect on the consolidated statements of changes in equity for the years ended December 31, 2014 and 2013, was a profit for \$364 (\$199, net of deferred income tax and ESPS) and a charge of \$874 (\$612, net of deferred tax), respectively.

(9) Securities under repurchase/resell agreements-

The debtor and creditor balances in respect of sale and purchase of repo transactions at December 31, 2014 and 2013, are analyzed as follows:

	<u>Purchaser</u>		<u>Seller</u>	
	<u>2014</u>	<u>2013</u>	<u>2014</u>	<u>2013</u>
Repo operations	\$ -	8,001	60,247	34,765
Collaterals sold or pledged	<u>-</u>	<u>(7,501)</u>	<u>-</u>	<u>-</u>
	\$ -	500	60,247	34,765
	=====	=====	=====	=====

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

Below is shown the type and total amount by type of asset of the collateral delivered as part of repo transactions and recorded as restricted securities as well as the securities received in repo transactions and the average terms of those open operations at December 31, 2014 and 2013:

	2014				2013			
	Reporting (restricted)	Reported (memorandum account)	Average term		Reporting (restricted)	Reported (memorandum account)	Average term	
			Sell	Purchase			Sell	Purchase
<u>Government securities</u>								
BONDES D	\$ 4,834	-	110	-	\$ 12,682	6,570	66	2
CETES	3,881	-	78	-	4	-	7	-
UMS	-	-	-	-	2,717	-	2,221	-
BPAG91	-	-	-	-	-	1,436	-	2
BONOS M	37,540	-	5	-	18,308	-	277	-
BPA 182	-	-	-	-	-	2	-	66
BREMS	14,302	-	38	-	-	-	-	-
<u>Bank notes</u>								
IBANOBRA	-	-	-	-	2,011	-	2	-
	\$ 60,557	-			\$ 35,722	8,008		
	=====	=====			=====	=====		

During the year ended December 31, 2014, interest income and expense from repo agreements, recognised in the consolidated income statement amounted to \$41 and \$2,152 respectively (\$565 and \$1,889, respectively in 2013) (refer to note 31).

(10) Collaterals sold or pledged as a guarantee-

At December 31, 2014 and 2013, the collateral received in stock borrowing transactions and sold or pledged as a guarantee is shown as follows:

	2014			2013		
	<u>Securities</u>	<u>Amount</u>	<u>Average term</u>	<u>Securities</u>	<u>Amount</u>	<u>Average term</u>
Cetes	399,858,134	\$ 3,947	58 days	401,961,572	\$ 3,928	2 days
Bonds	160,374,887	17,421	38 days	47,185,452	4,957	2 days
Udibonos	876,921	529	7 days	343,464	191	14 days
		\$ 21,897			\$ 9,076	
		=====			=====	

During the years ended December 31, 2014 and 2013, interest expense arising from securities lending transactions recognised in the consolidated statement of income, amounted to \$37 and \$22, respectively (refer to note 31).

(Continued)

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(11) Derivative transactions-

The Group's main objectives in executing derivative transactions are neutralizing market, credit and liquidity risks that may affect the entity's future results. These instruments are also offered to certain of our customers with the same intention. The execution of these transactions is in agreement with the policies established by HSBC Holding plc and with the authorization of the Central Bank. Valuation models are duly authorized and are proper for recognition of the risks involved.

Interest rate and foreign currency swaps represents that the Group and its customers interchange currencies and/or rates in the future. Options grant the right to receive or pay an interest rate or foreign currency at a determined price. Futures are a standard and mandatory agreement to buy or sell a predetermined amount of a specific tangible good (commodity) on a future day or date, pursuant to a standardized contract. The terms and conditions of derivative transactions of the Bank are in accordance with market standards.

The Group uses derivatives for hedging purposes (cash flows) to convert variable flows to fixed flows. This allows two risk types of hedged:

Interest rate risk - If the underlying instrument is an asset with variable interest rate, such interest is converted into fixed interest rate through an interest rate swap, by receiving a fixed flow and paying a variable flow. If the underlying instrument is a liability, it is converted into fixed interest rate through an interest rate swap, by receiving a variable flow and paying a fixed flow. The hedged risk is the risk attributable to changes in interest rates of the underlying instrument.

Foreign currency risk - Whether the underlying instrument is an asset or a liability, fixed interest denominated in another currency is translated into pesos by entering into a foreign currency swap. The hedged risk is the risk of changes in the functional currency equivalent to cash flows for a recognized foreign currency and measured by the spot exchange rate.

At December 31, 2014 and 2013, the Group had derivative-related financial assets, which amounted to \$80,041 and \$49,769, respectively. Such assets had the credit quality shown as follows:

<u>Risk level</u>	<u>2014</u>	<u>2013</u>
Low	\$ 67,471	42,145
Satisfactory	12,251	7,487
Significant	91	137
High	<u>228</u>	<u>-</u>
Total	\$ 80,041	49,769
	=====	=====

(Continued)

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The prospective effectiveness of the inception will be evaluated by comparing the critical terms of the hedged asset/liability, in connection with the hedging instruments. With this reconciliation and on this basis, the hedge is expected to be highly effective upon inception and over the life of the hedge.

Present effectiveness and prospective effectiveness of the life of the hedge will be evaluated at each month-end, by calculating the changes in cash flows of the derivative in all applicable periods in which the instrument has been designated as a hedge. These will be compared with changes in cash flows of the hedged item in the same period to which it applies.

The value of exposure to market risk of transactions with derivative financial instruments is included in the Value at Risk of HSBC's Global Market, which is explained in note 33.

If the primary position had not been hedged with the derivative financial transactions mentioned earlier, there would have been an adverse impact in the results of operations for 2014 of \$130 and a positive impact for \$27 in 2013.

Fair value hedges

In respect of fair value hedges, at December 31, 2014, hedging instrument losses and gains in respect of the hedged position were \$156 and \$177, respectively (\$456 and \$416, respectively in 2013).

Cash flow hedges

At December 31, 2014, the periods in which cashflows in respect of cashflow hedges are expected to occur are as follows:

	<u>2015</u>	<u>2016</u>	<u>2017</u>	<u>2018</u>	<u>2019</u>	<u>2020</u>
Interest rate swaps	\$ (533)	(634)	(419)	-	-	-
Currency swaps	<u>27</u>	<u>47</u>	<u>65</u>	<u>1,190</u>	<u>706</u>	<u>(818)</u>
	\$ (506)	(587)	(354)	1,190	706	(818)
	===	===	====	=====	===	===

The total amount recognised in comprehensive income during 2014 in respect to fair value changes in effective cash flow hedges was a profit of \$24 (profit of \$134 in 2013).

The amount reclassified from comprehensive income to the income statement for the years ended on December 31, 2014 and 2013 in respect of the unamortized fair value of re-designated hedges and in respect of the sale of the hedged positions (bonds) was a loss of \$5 and an income of \$44, respectively, which was registered in "Financial intermediation income".

(Continued)

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(Millions of pesos)

During 2014 and 2013 the amount reclassified from comprehensive income to the income statement for the respective years in respect of the amortization of the fair value of swaps re-designated from cash flow swaps to net interest income was an income of \$33 and a loss of \$50, respectively.

Compensation and net exposure to credit risk in derivatives

The Group has the right to compensate derivative transactions at the time of settlement under the ISDA (International Swaps and Derivatives Association) and CSA (Credit Support Annex) which have jointly agreed with its customers. The effect that this right of reimbursement had over the credit risk exposure at December 31, 2014 and 2013 was \$34,679 and \$21,502, respectively.

Notional amounts

Notional amounts of contracts represent the derivatives volume outstanding and not the potential gain or loss associated with the market risk or credit risk of such instruments. The notional amounts represent the amount to which a rate or price is applied for determining the amount of cash flows to be exchanged.

At December 31, 2014 and 2013, the Group did not provide non cash collateral in respect of derivative liabilities. Equally the Group did not receive any non cash collateral from derivative counterparties.

At December 31, 2014 and 2013, the credit risk (including collaterals) in respect of derivative financial instruments, amounted to \$18,859 and \$11,030, respectively.

During the years ended December 31, 2014 and 2013, the Group's counterparties had defaults originating from derivative transactions that amounted to \$162 and \$473 respectively. At December 31, 2014 and 2013, the balance in sundry debtors resulting from defaults in this type of amounted to \$1,675 and \$1,513 respectively of which \$1,507 as of December 31, 2014 were reserved (\$1,425 in 2013).

At December 31, 2014 and 2013, the fair value valuation of the derivative instruments is analyzed as shown in the following page.

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December 31, 2014

		Notionals								Fair Value								
		FX		Interest rate		Shares		Total		FX		Interest rate		Shares		Total		
		Purchase /	Sale /	Purchase /	Sale /	Purchase /	Sale /	Purchase /	Sale /	Balance /	Balance /	Balance /	Balance /	Balance /	Balance /	Balance /	Balance /	
		Asset	Liability	Asset	Liability	Asset	Liability	Asset	Liability	Asset	Liability	Asset	Liability	Asset	Liability	Asset	Liability	Net
Trading																		
Forwards	\$	524,595	524,465	45,730	42,730	5,153	5,153	575,478	572,348	18,504	18,107	379	377	170	170	19,053	18,654	399
Options		10,390	10,389	23,742	24,369	-	-	34,132	34,758	298	298	148	89	-	-	446	387	59
Swaps		176,874	173,340	1,381,493	1,462,862	-	-	1,558,367	1,636,202	31,993	31,218	28,472	29,790	-	-	60,465	61,008	(543)
		711,859	708,194	1,450,965	1,529,961	5,153	5,153	2,167,977	2,243,308	50,795	49,623	28,999	30,256	170	170	79,964	80,049	(85)
Hedge																		
Swaps		-	2,630	15,000	18,845	-	-	15,000	21,475	-	605	77	625	-	-	77	1,230	(1,153)
	\$	711,859	710,824	1,465,965	1,548,806	5,153	5,153	2,182,977	2,264,783	50,795	50,228	29,076	30,881	170	170	80,041	81,279	(1,238)

December 31, 2013

		Notionals								Fair Value								
		FX		Interest rate		Shares		Total		FX		Interest rate		Shares		Total		
		Purchase / Asset	Sale / Liability	Purchase / Asset	Sale / Liability	Purchase / Asset	Sale / Liability	Purchase / Asset	Sale / Liability	Balance / Asset	Balance / Liability	Balance / Asset	Balance / Liability	Balance / Asset	Balance / Liability	Balance / Asset	Balance / Liability	Net
Trading																		
Forwards	\$	328,123	326,720	20,000	16,500	301	301	348,424	343,521	3,505	2,407	36	32	45	45	3,586	2,484	1,102
Options		11,473	10,247	14,255	17,724	-	-	25,728	27,971	83	83	128	92	-	-	211	175	36
Swaps		185,873	169,287	1,145,009	1,178,378	-	-	1,330,882	1,347,665	18,896	16,965	26,908	27,229	-	-	45,804	44,194	1,610
		525,469	506,254	1,179,264	1,212,602	301	301	1,705,034	1,719,157	22,484	19,455	27,072	27,353	45	45	49,601	46,853	2,748
Hedge																		
Swaps		-	282	17,120	16,352	-	-	17,120	16,634	-	27	168	763	-	-	168	790	(622)
	\$	525,469	506,536	1,196,384	1,228,954	301	301	1,722,154	1,735,791	22,484	19,482	27,240	28,116	45	45	49,769	47,643	2,126

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GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

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(12) Loan portfolio-

At December 31, 2014 and 2013 the loan portfolio and the credit commitments are analyzed as follows:

	<u>2014</u>	<u>2013</u>
Total loan portfolio, shown in the consolidated balance sheet	\$ 231,460	204,990
Recorded in memorandum accounts (note 30a):		
Lending commitments	<u>33,874</u>	<u>25,561</u>
	\$ 265,334	230,551
	=====	=====

(a) Classification of current and past due loan portfolio by currency, rated portfolio, economic sector and by aging of past due loans-

At December 31, 2014 and 2013, the classification of current and past due loan portfolios by currency, which includes economic sector, rated portfolio and ageing of past due loans is shown in the following page.

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GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

December 31, 2014 and 2013

(Millions of pesos)

Portfolio	Commercial activity		Financial institutions		Government entities		Consumer		Residential mortgages		Total	
	2014	2013	2014	2013	2014	2013	2014	2013	2014	2013	2014	2013
Current:												
Pesos	\$ 86,370	83,048	9,648	4,219	32,133	18,068	36,371	37,675	25,003	23,415	189,525	166,425
Foreign currency	28,204	25,159	230	120	408	65	-	-	-	-	28,842	25,344
UDIS	-	-	-	-	-	-	-	-	850	1,065	850	1,065
Total	114,574	108,207	9,878	4,339	32,541	18,133	36,371	37,675	25,853	24,480	219,217	192,834
Past due:												
Pesos	9,764	8,919	-	3	85	45	1,568	1,788	444	574	11,861	11,329
Foreign currency	253	698	-	-	-	-	-	-	-	-	253	698
UDIS	-	-	-	-	-	-	-	-	129	129	129	129
Total	10,017	9,617	-	3	85	45	1,568	1,788	573	703	12,243	12,156
Total:												
Pesos	96,134	91,967	9,648	4,222	32,218	18,113	37,939	39,463	25,447	23,989	201,386	177,754
Foreign currency	28,457	25,857	230	120	408	65	-	-	-	-	29,095	26,042
UDIS	-	-	-	-	-	-	-	-	979	1,194	979	1,194
Total	\$ 124,591	117,824	9,878	4,342	32,626	18,178	37,939	39,463	26,426	25,183	231,460	204,990
Classification by activity												
Manufacturing	\$ 67,909	63,109	-	-	-	-	-	-	-	-	67,909	63,109
Agriculture, forestry and fishing	9,955	10,596	-	-	-	-	-	-	-	-	9,955	10,596
Trade and tourism	18,906	21,249	-	-	-	-	-	-	-	-	18,906	21,249
Services	27,821	22,870	-	-	-	-	-	-	-	-	27,821	22,870
Financial services	-	-	4,638	2,074	-	-	-	-	-	-	4,638	2,074
Credit Unions	-	-	994	1,046	-	-	-	-	-	-	994	1,046
Municipalities	-	-	-	-	890	1,085	-	-	-	-	890	1,085
States	-	-	-	-	9,234	7,636	-	-	-	-	9,234	7,636
Credit to the Federal Government (support programs)	-	-	-	-	256	386	-	-	-	-	256	386
Other government entities (see note 12a)	-	-	-	-	22,246	9,071	-	-	-	-	22,246	9,071
Others to financial organizations	-	-	4,246	1,222	-	-	-	-	-	-	4,246	1,222
Automobile credit	-	-	-	-	-	-	2,230	2,479	-	-	2,230	2,479
Credit Card	-	-	-	-	-	-	19,445	19,115	-	-	19,445	19,115
Multicredit	-	-	-	-	-	-	15,382	15,808	-	-	15,382	15,808
Fixed payment	-	-	-	-	-	-	882	2,061	-	-	882	2,061
Construction and housing	-	-	-	-	-	-	-	-	26,426	25,183	26,426	25,183
Total	\$ 124,591	117,824	9,878	4,342	32,626	18,178	37,939	39,463	26,426	25,183	231,460	204,990
Past due loans by aging												
From 1 to 180 days	\$ 1,263	2,448	-	-	35	45	1,555	1,778	398	518	3,252	4,789
From 181 to 365 days	1,087	5,927	-	3	31	-	13	10	71	106	1,201	6,046
From 1 to 2 years	7,177	74	-	-	19	-	-	-	28	51	7,224	125
More than 2 years	490	1,168	-	-	-	-	-	-	76	28	566	1,196
Total	\$ 10,017	9,617	-	3	85	45	1,568	1,788	573	703	12,243	12,156
NOTE: The amounts above are for cumulative amounts of principal (for 2014 \$230,418 and 2013 \$203,890) and interest (for 2014 \$1,042 and 2013 \$1,100) which are classified in the consolidated balance sheets of the Group as assets under the caption of current and past due loans.												
Loan portfolio rated	2014	2013	2014	2013	2014	2013	2014	2013	2014	2013	2014	2013
Portfolio rating risk												
A-1 and A-2	121,140	110,258	6,036	2,677	23,134	10,542	3,019	2,721	23,915	22,244	177,244	148,442
B-1, B-2 and B-3	23,758	18,801	3,456	1,665	6,333	4,191	31,138	32,226	2,175	2,526	66,860	59,409
C-1 and C-2	2,700	3,888	356	-	2,882	2,833	2,104	2,644	320	401	8,362	9,766
D-High	7,346	8,942	30	-	85	228	1,611	1,816	11	12	9,083	10,998
E-Irrecoverable	3,522	1,496	-	-	-	-	67	56	4	-	3,593	1,552
Total portfolio rated	158,466	143,385	9,878	4,342	32,434	17,794	37,939	39,463	26,425	25,183	265,142	230,167
Exempt portfolio	-	-	-	-	192	384	-	-	-	-	192	384
Total portfolio	\$ 158,466	143,385	9,878	4,342	32,626	18,178	37,939	39,463	26,425	25,183	265,334	230,551
Allowance and percentage												
A-1 and A-2	\$ 681	600	58	15	121	59	28	25	66	65	954	764
B-1, B-2 and B-3	510	423	87	79	149	125	2,140	2,327	135	154	3,021	3,108
C-1 and C-2	229	316	23	-	182	207	760	984	156	172	1,350	1,679
D-High	3,071	4,108	6	-	39	67	1,205	1,365	7	8	4,328	5,548
E-Irrecoverable	2,731	803	-	-	-	-	68	56	4	-	2,803	859
	7,222	6,250	174	94	491	458	4,201	4,757	368	399	12,456	11,958
Additional reserves	102	121	-	-	-	-	119	129	16	15	237	265
Total	\$ 7,324	6,371	174	94	491	458	4,320	4,886	384	414	12,693	12,223
General and specific allowances												
General	\$ 681	600	58	15	121	59	29	25	73	71	962	770
Specific	6,643	5,771	116	79	370	399	4,291	4,861	311	343	11,731	11,453
Total	\$ 7,324	6,371	174	94	491	458	4,320	4,886	384	414	12,693	12,223

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Unsecured loans to IPAB:

On September 27, 2002, the Group granted a \$47,357 (nominal) loan to IPAB. The loan was documented by a promissory note that may only be endorsed to the Central Bank as a guarantee for the note amount. In addition, on May 12, 2005, the Group granted to IPAB an unsecured loan for a total nominal amount of \$5,000. Finally on May 31, 2007, the Group and IPAB signed a new agreement to document the consolidated principal outstanding balance as of that date amounting to of \$29,058. In accordance to the aforementioned agreement, the total balance was split into four tranches of \$7,265 each, which mature between May and December 2013, payments in advance are permitted. Each tranche bears interest at an annual rate equal to the annual yield rates of 28-days CETES plus 56 basis points. At December 31, 2013 the four loan tranches had been settled in accordance with the maturity dates set forth in the debt recognition agreement.

Federal Government support programs:

As a result of the economic crisis in 1995, the Federal Government and the Mexican Bankers' Association established loan support programs and agreements with debtors of credit institutions named Additional Benefits to Housing Loan Debtors (BADCV, for its acronym in Spanish).

The financial support programs and agreements consist of discounts granted to debtors, which are generally absorbed proportionately by the Federal Government and the Group, in accordance with the terms of each program. These discounts were applied in each payment of the loans subject to the program. On July 15, 2010, the Bank signed an agreement with the Federal Government for an early termination of the support programs for housing loans. This early termination scheme (ETA, for its acronym in Spanish) consisted that the qualified loans received on or before December 31, 2010 the benefit of the discount on the unpaid balance of the loan. The discount absorbed by the Federal Government will be paid to the Bank in five equal installments, the first in December 2011 and the rest in the months of June of the years 2012-2015, to which they will add a financial cost, based on the 91 days treasury certificates rate. The payment of each installment is subject to the delivery of a series of reports to the Banking Commission. As of December 31, 2014 and 2013, the amount receivable from the Federal Government in connection with discounts granted and the costs related to the Bank and the ETA are analyzed as follows:

	<u>2014</u>		<u>2013</u>	
	<u>Portfolio</u>	<u>Cost</u>	<u>Portfolio</u>	<u>Cost</u>
ETA/BADCV	\$ 192	3	386	3
	===	==	===	==

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The discounts related to the early termination agreement are shown as follows:

	In charge to	
	<u>Financial Group</u>	<u>Federal Government</u>
Discounts granted originally	\$ 457	973
Additional discount granted by the Group	<u>93</u>	<u>-</u>
Discount granted at December 31, 2010	550	973
Discounts to unallowed credits ^(a)	(2)	(3)
Discounts of credits that did not demonstrated compliance with payment ^(b)	(12)	(26)
Restructured loans under the agreement formalized up to the cut-off date	<u>(1)</u>	<u>-</u>
Total discounts granted at December 31, 2011	535	944
Total additional discounts granted by the Bank that did not belong to ETA	<u>(93)</u>	<u>-</u>
Total additional discounts granted by the Bank that belong to ETA	\$ 442	944
	====	====

^(a) Through communications issued in April 2011, the Banking Commission requested the replacement of the exhibits for the year ended on December 31, 2010, and subsequently, during the issuance of the report on the correct application (ETA report) on September 29, 2011, where the portfolio balances and the related discounts decreased for, with 28 credits defined as not subject to the ETA, 24 of which were benefited from the Discount Program.

^(b) This corresponds to the credit discounts that as of March 31, 2011 did not demonstrate a compliance with the payment and that would had been chargeable to the Federal Government, in the event of complying with such condition.

As of December 31, 2010, the discount related to the Federal Government was reclassified to be presented as part of the accounts receivable from the Federal Government which are part of the current loans portfolio with government entities; the corresponding amount of discount related to the Group was cancelled against the allowance for loan losses, in accordance with the special accounting criteria issued by the Banking Commission.

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A reconciliation of movements in the allowance for loan losses related to the conditioned discount covered by the Group is shown below:

Opening balance as of December 31, 2010	\$	70
Debt forgiveness, discounts and/or rebates		(2)
Conditioned discount assigned to the Bank		(550)
Allowance charged to the consolidated statement of operations		<u>496</u>
Final balance	\$	<u>14</u> ===

Determination of obligations of the Federal Government:

The final base amount determined through the ETA Report is \$944, divided in five installments of \$189 each. At December 31, 2014, four loan tranches have been settled and the remaining installment will be payable on the first banking day of June 2015. Accordingly, the balance receivable as of December 31, 2014 and 2013 by ETA amounts to \$189 and \$378, respectively, of principal, plus \$3 and \$8 corresponding to the accrued not collected financial cost.

The discounts granted due from the Government in Mexican pesos or UDIS related to those credits that should have shown sustained payment by March 31, 2011, according to the agreement, amounts to \$167 at December 31, 2010.

There were no discount in charge to the Government related to credits in UDIS for which they received prior discounts over the outstanding balance before they were incorporated in to the "Discount program", as referred at the numeral 3.1.2 of the Circular 1430 issued by the Banking Commission.

At December 31, 2010 there were some clients that did not meet the requirements to be incorporated into to ETA. However, in accordance with the actual rules it is still possible that they will subsequently be incorporated in to the program; in such case the Group must have to absorb 100% of the discount granted. The maximum amount of discount that the Group would absorb for these credits at December 31, 2014 and 2013, amount to \$14 and \$7, respectively.

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The numbers of securities related to BADCV that are held by the Group at December 31, 2014 and 2013 are shown as follows:

<u>Program</u>	<u>Trust Program</u>	<u>Number</u>	<u>Due date</u>	<u>Special CETES</u>	<u>Special “C” CETES</u>
Programs to support Debtors of mortgage credits	421-5	20 Years	13/07/2017	12,549,378	766,145
	422-9	25 Years	07/07/2022	5,772,652	184,517
	423-2	30 Years	01/07/2027	30,074,223	-
Program to support the construction of houses in the stage of individualiza credits		25 Years - from 230 to 330 thousand			
	432-6	Udis	11/08/2022	74,389	50,693

(b) *Program for the support of people affected by tropical storm Manuel, Odile and hurricane Ingrid:*

Due to the natural disasters caused by the hydro-meteorological events “Ingrid” and “Manuel” in 2013 and “Odile” in September 2014, that affected several Mexico locations and with a view to supporting borrowers who were affected by such natural phenomena while trying to promote the stability of credit institutions, through official document P065/2013 dated October 18, 2013 and P110/2014 dated September 19, 2014, the Banking Commission authorized the country’s credit institutions certain special accounting criteria applicable to loans of customers with domiciles or source of payment of their loans in locations in the Mexican Republic that were declared in emergency or natural disaster by the Ministry of the Interior through publication in the DOF during the months of September and October 2013 and September 2014. The authorized accounting criteria refer to not considering as past due or restructured portfolio in accordance with paragraphs 58 to 63 of the criterion B-6 to the annex 33 of the Provisions, the loans to which the benefit referred to in the following paragraph is applied, provided the following is complied: 1) the loan was recognized as performing at the date such events hit; 2) the restructuring or renovation procedures end by 120 natural days after the date such events hit; and 3) the new maturity of is not greater than three months after the date on which the loans became due and payable.

The benefit offered by the Group to its customers who so request consists of the total deferral of their payments for up to three months. The program applies for mortgage-backed housing loans, automobile loans, personal loans, payroll loans, credit cards and PYME loans.

At December 31, 2014, the amount that would have been recorded and presented on the consolidated balance sheet and in the consolidated statement of income, had the special accounting criteria authorized by the Banking Commission not been applied, which relates to interest, was \$2 (not material for 2013).

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

Since the benefit applied by the Group consisted only of the deferral of the payment of principal and interest thereon for up to 3 months, it was not necessary to make any entries in the accounting associated with the application of this disaster relief program.

(c) Additional loan portfolio information-Commission by type of loan:

For the years ended at December 31, 2014 and 2013, commissions by type of loan included in commissions and fees collected within the consolidated statements of income, are presented in as follows:

	Amount	
	<u>2014</u>	<u>2013</u>
Commercial	\$ 308	293
Consumer	2,647	2,679
Mortgage	<u>51</u>	<u>48</u>
Total	\$ 3,006	3,020
	=====	=====

Below shows the increases in deferred credits account for the initial granting of credits for the years ended at December 31, 2014 and 2013.

	Amount Commissions	
	<u>2014</u>	<u>2013</u>
Consumer	\$ 208	162
Commercial	82	93
Mortgage	<u>23</u>	<u>69</u>
Total	\$ 313	324
	===	===

During the years ended at December 31, 2014 and 2013, \$246 and \$210, respectively, were recorded corresponding to the accrued commissions by the initial granting of credits of the period, using the straight line method, which were registered in the line "Interest Income" in the consolidated statement of income. The average weighted period (in months) for such commissions and fees are shown in the following page.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

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	<u>2014</u>	<u>2013</u>
Commercial	39	31
Consumer	49	35
Credit cards	12	12
Mortgage	212	201
	===	===

The initial costs and expenses for the issuance of credits related to the years ended December 31, 2014 and 2013 amounts to \$69 and \$157, respectively. These amounts relate to payment of commissions and underwriting credits.

Annual weighted lending rates:

During 2014 and 2013, the annual weighted lending rates (unaudited information) were as shown below:

	<u>2014</u>	<u>2013</u>
Commercial loans	7.93%	7.80%
Financial entities	5.47%	5.12%
Personal loans	20.20%	26.85%
Mortgages loans	9.59%	9.91%
Government entities	5.21%	5.96%

Loans discounted with recourse:

Mexican Government has established certain funds to promote the development of specific areas of agriculture, cattle ranching, industrial and tourism sectors, which are managed mainly by the Central Bank, Nacional Financiera SNC (a national development bank, NAFIN), the National Foreign Trade Bank, and the Guarantee Fund for Agricultural Development by discounting loans with recourse.

At December 31, 2014 and 2013, the amount of loans granted under these programmes amounted to \$12,886 and \$10,062, respectively, and the related liability is included in "Due to banks and other institutions" (refer to note 22).

(Continued)

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Restructured and renewed loans:

At December 31, 2014 and 2013, restructured and renewed loans are analyzed as follows:

	2014			
	Renewed and restructured portfolio			Modified not considered as restructured ⁽⁴⁾
	Past due restructured ⁽¹⁾	Transfer to past due ⁽²⁾	Stayed current ⁽³⁾	
Commercial loans	\$ 1,706	341	8,298	906
Government entities	-	1,343	-	-
Consumer loans	34	-	87	-
Credit card	129	-	235	-
Mortgage loans	<u>62</u>	<u>-</u>	<u>665</u>	<u>-</u>
	\$ 1,931	1,684	9,285	906
	=====	=====	=====	=====

	2013			
	Renewed and restructured portfolio			Modified not considered as restructured ⁽⁴⁾
	Past due restructured ⁽¹⁾	Transfer to past due ⁽²⁾	Stayed current ⁽³⁾	
Commercial loans	\$ 1,143	624	3,338	6,181
Government entities	-	1,325	-	-
Consumer loans	19	-	55	-
Credit card	106	-	314	-
Mortgage loans	<u>143</u>	<u>-</u>	<u>669</u>	<u>-</u>
	\$ 1,411	1,949	4,376	6,181
	=====	=====	=====	=====

(1) Nonperforming loans that was restructured or renewed.

(2) Restructuring or renewals of loans with a single payment of principal at maturity and periodic interest payments and credits with a single payment of principal and interest at maturity, which were transferred to past due loans for been restructured or renewed.

(3) Restructured or renewed loans that remained in current portfolio under paragraphs 59 to 63 of Criteria B-6 "loan portfolio" of Annex 33 of the Provisions.

(4) Modified loans that were not considered as restructured according to paragraph 64 of Criteria B-6 "loan portfolio" of Annex 33 of the Provisions.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

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For the years ended December 31, 2014 and 2013, the amount of interest income recognised due to the restructuring of overdue loans was \$1 each year. In respect of loans to small and medium enterprises in the commercial portfolio, with the aim of reducing the level of the Bank's credit risk, there is an agreement with Nacional Financiera, S. N. C. (NAFIN) to promote this type of credits, where NAFIN supports up to 50%, 90% or 100% of the loan granted depending on the applicable program. For the years ended December 31, 2014 and 2013, NAFIN supported \$3,689 and \$3,874, respectively.

Restructuring processes entail the granting of a reduction in interest rates, a waiting period for complying with the payment obligations, the cancellation of any portion of capital, default interest and commissions. At December 31, 2014 and 2013, debts cancelled totaled \$5 and \$27, respectively. Sometimes, in the restructuring process additional guarantees such as mortgage guarantees are obtained. At December 31, 2014, the value of such additional guarantees aggregates \$397 (\$137 in 2013).

Past due loan portfolio

Nominal interest that would have accrued in 2014 from the past due loan portfolio amounted to \$276 (\$221 in 2013).

An analysis of the annual movement of past due loans for the years ended December 31, 2014 and 2013, is shown as follows:

	<u>2014</u>	<u>2013</u>
Balance at beginning of year	\$ 12,156	4,013
Transfers from current to past due loan portfolio	23,812	23,922
Transfers to current loan portfolio by restructures and renewals	(238)	(335)
Credits collected:		
Cash collections	(8,622)	(4,287)
Collection in kind	(2)	(15)
Write offs	(7,474)	(5,356)
Transfer to current loan portfolio	(7,495)	(5,800)
Foreign exchange	<u>106</u>	<u>14</u>
Balance at end of year	\$ 12,243 =====	12,156 =====

During 2014 and 2013, there were no write-offs of loans granted to related parties.

(Continued)

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As of December 31, 2014, there were no loans in the current portfolio to continue receiving any payments in accordance with section VIII of article 43 of the Commercial Insolvency and Bankruptcy Law ("CIBL"), or loans that were granted in accordance with article 75, relating to sections II and III of article 224 of the Commercial Insolvency and Bankruptcy Law.

For the year ended December 31, 2014, the amount of recoveries of loans that were previously written-off amounted \$780 (\$760 in 2013).

Impaired loans:

At December 31, 2014 and 2013, the balance of impaired commercial loans is \$10,983 and \$10,665 respectively, from which \$1,544 and \$1,096 are recorded as current loans and \$9,439 and \$9,569 as past due loans, respectively.

Risk concentration:

As of December 31, 2014 and 2013, the Group maintains three loans that exceeded the 10% limit of its basic capital at December 31, 2014 and September 30, 2013 of \$4,159 and \$4,313, respectively. These loans represent the three main debtors of the Bank amounting to \$23,692 (\$12,067 in 2013) that represents the 56.96% (27.98% in 2013) of the basic capital.

Securitisation of mortgage portfolio:

Outstanding securitisation transactions as of December 31, 2014 and 2013, relate to transactions undertaken in 2008 and 2007, by means of transferring of all of the Bank's risks and rewards of such mortgage portfolio without reserves or limitations in favour of three Trusts (used as a securitization vehicle). The Trusts issued certificates that were acquired by the public and a subordinated trust acknowledgment, which gives the Group the right to receive any remaining funds of the Trust. The Trust note is recorded on the "Benefits receivable on securitization transactions" caption on the consolidated balance sheet.

The amounts of the portfolio that was sold in the market, as well as the conditions of the certificates issued by the stockmarket certificate issued by the Invex Trusts are as follows:

Invex	Date of issuance	Nominal portfolio sold	Cash received	Acknowledgment	Maturity date	Stockmarket certificates interest rate			
						Series "A"	Series "B"	Series "A1"	Series "B1"
I	22-mar-07	\$ 2,525	2,474	25	1 to 30 years	8.24%	9.58%	-	-
II	2-oct-07	3,538	3,457	36	2025	8.80%	10.11%	-	-
III	4-sep-08	1,663	1,483	163	2028	-	-	9.99%	10.16%
		=====	=====	=====		=====	=====	=====	=====

The Group acquired the subordinated trust acknowledgments, which grant the right to any remainder of the mortgage portfolio upon payment of the amounts due under the certificates.

(Continued)

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As of December 31, 2014 and 2013, the book value of the subordinated trust acknowledgments are recognized in “Benefits receivable on securitization transactions” and is analyzed as follows:

		<u>2014</u>	<u>2013</u>
Original amount of the certificates	\$	224	224
Recoveries of the values of acknowledgements		(41)	(2)
Valuation		<u>(36)</u>	<u>(40)</u>
Trust certificates net value	\$	147	182
		====	====

The result of acknowledgment valuations is determined considering the fair value of the notes issued by the trustee, which is obtained through a price vendor.

In the event that the total amount due of the certificates is less than 10% of the par value of the total amount of the certificates on the date of the offering, the Bank shall have the option to repurchase the remaining portfolio of the trust and with such proceeds the outstanding certificates would be repaid.

The Group executed a service provision agreement, through which the Bank provides the administration and collection of the mortgage portfolio sold in the market, in exchange for a commercial commission.

(d) Allowance for loan losses -

As explained in notes 3(l) and 33, an allowance is established to provide for credit risks associated with the collection of the Group’s loan portfolio.

At December 31, 2014 and 2013 the allowance for loan losses, analyzed in section (a) of this note is shown below:

		<u>2014</u>	<u>2013</u>
Rated loan estimate	\$	12,456	11,958
Additional reserves, including past due interest		<u>237</u>	<u>265</u>
Total allowance for loan losses	\$	12,693	12,223
		=====	=====

(Continued)

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Notes to Consolidated Financial Statements

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The classification by risk grade of the commercial portfolio, financial entities and government entities credit reserves at December 31, 2014 and 2013, is as follows:

		<u>2014</u>	<u>2013</u>
A-1	\$	511	447
A-2		393	227
B-1		262	211
B-2		234	132
B-3		250	284
C-1		367	423
C-2		67	100
D		3,155	4,283
E		<u>2,750</u>	<u>816</u>
	\$	7,989	6,923
		=====	=====

The following is an analysis of the movements of the allowance for the years ended December, 31, 2014 and 2013:

		<u>2014</u>	<u>2013</u>
Balance at beginning of year	\$	12,223	9,381
Increase charged to income		7,903	8,083
Exchange rate valuation effects		99	3
Effect on stockholders equity by the change in the methodology for financial entities (note 4) and for commercial portfolio in 2013 (note 3 (l))		30	799
Reverse of excess in allowance for loan losses (note 31 (c))		(32)	(6)
Applications*:			
Write-offs		(6,854)	(5,765)
Debt forgiveness		<u>(676)</u>	<u>(272)</u>
Balance at end of year	\$	<u>12,693</u>	<u>12,223</u>
		=====	=====

*Include \$56 of claim reductions from current portfolio.

(e) Sale of written-off portfolio-

During 2014 and 2013 the Bank did not sale previously written off portfolio.

The Group's credit policies are disclosed in note 34.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

(f) Credit portfolio transfer-

During 2014, the Financial Group transfer past due loan portfolio totaling to \$245 and recognized a related loss of \$215 within the caption of "Other net operating income" (see note 31(c)).

(13) Accounts receivable from reinsurance companies and insurance and bonding institutions-

As of December 31, 2014 and 2013, accounts receivable from reinsurance companies and insurance and bonding institutions include the following:

	<u>2014</u>	<u>2013</u>
Reinsurance companies' share of outstanding claims	\$ 59	73
Policy loans and receivables interest	58	18
	==	==

(14) Other accounts receivable-

At December 31, 2014 and 2013, other accounts receivable are analyzed as follows:

	<u>2014</u>	<u>2013</u>
Debtors on settlement transactions	\$ 14,667	29,157
Due from employees	2,897	3,103
Granted collaterals in cash	15,354	6,167
Other debtors	3,256	3,233
Preventive estimations	<u>(1,340)</u>	<u>(1,256)</u>
	\$ 34,834	40,404
	=====	=====

The balance of settlement accounts recorded under other accounts payable at December 31, 2014 and 2013 was \$16,868 and \$37,659, respectively, and recognized in the accounting item of "Settlement transactions".

(15) Foreclosed assets-

As of December 31, 2014 and 2013, foreclosed assets or assets received in lieu of payment are analyzed in the following page.

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Notes to Consolidated Financial Statements

(Millions of pesos)

	<u>2014</u>		<u>2013</u>	
	<u>Amount</u>	<u>Reserve</u>	<u>Amount</u>	<u>Reserve</u>
Property:				
Land	\$ 11	(8)	10	(6)
Buildings	<u>128</u>	<u>(58)</u>	<u>216</u>	<u>(61)</u>
	<u>139</u>	<u>(66)</u>	<u>226</u>	<u>(67)</u>
	\$ 73		159	
	==		===	

The charge to the income is related to the valuation reserve of foreclosed assets in 2014 which amounted to \$25 (\$27 in 2013).

The total foreclosed property includes constructions recorded as restricted assets due to the sale executed via reservation of title agreement, which amounts to \$7, with a reserve for \$3 generated at December 31, 2014 (\$9 and \$5, respectively in 2013).

During the years ended December 31, 2014 and 2013, the Group sold foreclosed assets with a book value of \$86 and \$69, respectively.

(16) Property, furniture and equipment-

Property, furniture and equipment at December 31, 2014 and 2013 are analyzed as follows:

	<u>2014</u>	<u>2013</u>	<u>Annual depreciation and amortization rate</u>	<u>Useful life in years</u>
Property	\$ 2,215	2,214	2% a 5%	20-50
Office furniture and equipment	1,458	1,474	10%	10
Computer equipment	4,055	4,006	Various	3 a 7
Transportation equipment	57	6	25%	4
Installation expenses	5,003	5,031	5% y 10%	10 a 20
Other equipment	<u>2,706</u>	<u>2,475</u>	Various	
	15,494	15,206		
Accumulated depreciation and amortization	(9,773)	(8,768)		
Accumulated impairment	<u>(64)</u>	<u>-</u>		
	5,657	6,438		
Land	<u>489</u>	<u>489</u>		
	\$ 6,146	6,927		
	=====	=====		

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

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For the year ended December 31, 2014, an impairment loss of \$64 was recognized. This amount was recorded in the consolidated statements of income under the caption of “Administrative and promotion expenses”.

Depreciation and amortization charged to the consolidated statement of income in 2014 and 2013 amounted to \$1,280 and \$1,274, respectively.

As a result of the conduction of a physical inventory of Group owned assets during 2014 and 2013, a negative adjustment was recorded in the year ended on December 31, 2014 in their net book value of \$42 (\$86 in 2013), which was recognized in the year’s income under “Other operating income, net”.

During the years ended at December 31, 2014 and 2013 several properties were sold with a book value of \$7 and \$5, respectively, generating a profit of \$20 and \$1, respectively, which were recorded as “Other operating income” (refer to note 31(c)).

(17) Equity investments-

Investments in associates and other permanent investments

At December 31, 2014 and 2013, permanent investments in shares classified by activity, are analyzed as follows:

	<u>2014</u>	<u>2013</u>
Associated and affiliated companies:		
Supplementary banking services	\$ 126	122
Mutual funds	94	94
Security and protection	<u>6</u>	<u>5</u>
	226	221
Other equity investments	<u>13</u>	<u>13</u>
	\$ <u>239</u>	<u>234</u>
	===	===

The recognition of the equity in the results of associated and affiliated companies represented a profit of \$49 in 2014 (\$43 in 2013).

During the years ended December 31, 2014 and 2013, the Group received dividends from its associated companies for \$37 and \$34, respectively.

(Continued)

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Notes to Consolidated Financial Statements

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(18) Long-term assets available for sale-

On August 21, 2013, the Financial Group entered into a contract to sell the Bonding Company to Afianzadora Aserta, S. A. de C. V. Grupo Financiero Aserta subject to the authorization from the corresponding authorities. This transaction was authorized on December 13, 2013, and the sales price was \$130, resulting in a loss before taxes of \$136 for the Financial Group, which was recorded in the consolidated statement of income for the year ended December 31, 2013 within “Discontinued operations”.

Therefore, through the sale authorization date and in accordance with the accounting criteria, the Bonding Company’s assets and liabilities were reclassified to “long-term assets, available for sale” in the consolidated balance sheet. Furthermore, the results of this transaction for the period from January 1 through December 13, 2013 were reclassified to be presented as discontinued operations within the consolidated statement of income.

On March 7, 2012, the Insurance Company and AXA Seguros, S.A. de C.V. (AXA) entered into a purchase and sale contract of certain assets whereby the Insurance Company agreed to transfer to AXA assets consisting of auto and damage insurance contracts. On October 25, 2012, the tax authorities authorized the transaction, except for the insurance policies for the coverage of risks inherent to the Financial Group and those policies of the same branch issued under the coinsurance contract with Mapfre Tepeyac, S. A. The Financial Group decided to discontinue the coinsurance policies mentioned above. Net income from the sale of damage and auto portfolios amounted to \$386 and was recorded in “Discontinued operations” in the consolidated statement of income as at December 31, 2013. Therefore, the Insurance Company’s damage insurance assets and liabilities as of December 31, 2013 were reclassified to “Long-term assets, available for sale” in the consolidated balance sheet in accordance with the accounting criteria. Moreover, the statements of income of this transaction for the years ended December 31, 2013 were reclassified to be presented as discontinued operations.

As of December 31, 2013, net assets from discontinued operations for the discontinuation of the Insurance Company’s damage and auto insurance branches, as mentioned in the above paragraph, are analyzed in the following page.

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(Millions of pesos)

Assets

Investment in securities	\$	72
Premium debtors (net)		6
Accounts receivable from reinsurers and re-guarantee (net)		4
Other assets, deferred charges and Intangible assets		3
Goodwill		<u>2</u>
Total assets		<u>87</u>

Liabilities

Technical reserves	(44)
Accounts payable to reinsurers And re-guarantee (net) (liability)	-
Sundry creditors and other accounts payable	(13)
Deferred credits	<u>-</u>
Total liabilities	<u>(57)</u>
	\$ 30
Total assets net	==

In addition to the discontinued operations mentioned above, as of December 31, 2013, \$5 corresponding to a property owned by the Bank, which sale was completed in 2014 were included in “Long-term assets available for sale”.

The effects of discontinued operations in the consolidated statements of income for the year ended December 31, 2013 were as follows:

		2013			
		<u>Group</u>	<u>Bonding Company</u>	<u>Insurance Company</u>	<u>Total</u>
Interest income	\$	-	21	13	34
Premiums income, net		-	17	114	131
Technical reserves		-	5	90	95
Claims and other contractual obligations		-	(15)	(98)	(113)
Commission and fee income		-	9	3	12
Financial intermediation		-	-	5	5
Other operating income		-	8	(28)	(20)
Cancellation of goodwill from sale of insurance		(168)	-	-	(168)
Loss on sale of Bonding Company		(136)	-	-	(136)
Gain on sale of insurance		-	-	386	386
Administrative and promotional expenses		-	(13)	125	112
Current income taxes		-	(11)	(143)	(154)
Deferred income tax		<u>-</u>	<u>-</u>	<u>2</u>	<u>2</u>
Discontinued operations	\$	(304)	21	469	186
		===	===	===	===

(Continued)

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For the year ended December 31, 2014, the Financial Group recorded \$150 in discontinued operations, corresponding to a legal contingency of the Bonding Company.

For the year ended December 31, 2014, the profit relating to the discontinuance of the operation associated with the Mapfre agreement amounted to \$39 and, at December 31, 2014, the Financial Group wrote-off goodwill for \$2, corresponding to such agreement.

(19) Other assets, deferred charges and intangibles assets-

At December 31, 2014 and 2013 other assets deferred charges and intangibles assets include:

	<u>2014</u>	<u>2013</u>
Recoverable taxes	\$ 562	734
Pre-paid labour obligations (note 24)	916	1,084
Pre-paid services and commissions	604	804
Software, net	1,135	1,026
Other intangible assets, net	<u>93</u>	<u>185</u>
	3,310	3,833
Goodwill from the Insurance Company	<u>1,047</u>	<u>1,047</u>
	\$ 4,357	4,880
	=====	=====

The movement for the years ended at December 31, 2014 and 2013 of other assets, deferred charges and intangible assets are analyzed as follows:

	<u>2014</u>	<u>2013</u>
Balance at beginning of year	\$ 4,880	4,243
Movements for the year from:		
Taxes	(332)	685
Software (*)	376	438
Software impairment	-	(47)
Software amortization for the year	(266)	(152)
Prepaid expenses	(174)	(128)
Others	<u>(127)</u>	<u>(463)</u>
	\$ 4,357	4,880
	=====	=====

(*) Software developed internally, which is amortized over a five-year period.

(Continued)

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At December 31, 2013 impairment losses of \$47, were recorded in the consolidated statement of income within the “Other operating income” caption.

Intangible assets that are shown in the consolidated balance sheet do not include any restriction, are not considered as debt guaranty; there are no contractual commitments, related to the acquisition thereof.

(20) Deposits funding-

The weighted average deposit rates (unaudited) for the years ended December 31, 2014 and 2013 are analyzed as follows:

	2014			2013		
	<u>Pesos</u>	<u>Dollars</u>	<u>UDIS</u>	<u>Pesos</u>	<u>Dollars</u>	<u>UDIS</u>
Demand deposits	0.70	0.05	-	0.92	0.05	-
Time deposits	2.82	0.11	0.12	3.41	0.19	0.16
	=====	=====	=====	=====	=====	=====

During December 2014, the Financial Group throughout the Bank placed six issuances of Bonds (CEDES) amounting to \$22,450, bearing monthly interest at the TIIE rate shown as follows:

<u>Series</u>	<u>Issuance</u>	<u>Coupon rate (1)</u>	<u>Maturity date</u>
14001	\$ 4,600	TIIE + 5 bps	June 2015
14002	7,000	TIIE - 3 bps	March 2015
14003	5,200	TIIE	March 2015
14004	950	TIIE + 5 bps	June 2015
14005	700	TIIE + 5 bps	June 2015
14006	<u>4,000</u>	TIIE	March 2015
	22,450		
Accrued Interest	<u>24</u>		
	\$ 22,474		
	=====		

*(1) bps - basis points

(Continued)

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Notes to Consolidated Financial Statements

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(21) Bank bonds-

At December 31, 2014 and 2013, the Group has made the following issuances under the bank bonds program:

<u>Issuance day</u>	<u>Reference rate</u>	<u>Maturity day</u>		<u>2014</u>	<u>2013</u>
May 10, 2006 ⁽²⁾	9.08%	April 27, 2016	\$	1,000	1,000
December 9, 2013 ⁽¹⁾	TIIE + 0.3 pp	December 3, 2018		2,300	2,300
December 9, 2013 ⁽²⁾		November 27, 2023		2,700	2,700
November 26, 2014 ⁽³⁾	N/A	January 2, 2015		50	-
December 10, 2014 ⁽³⁾	N/A	January 16, 2015		73	-
December 17, 2014 ⁽³⁾	N/A	January 23, 2015		<u>74</u>	<u>-</u>
			\$	6,197	6,000
Accrued Interest				<u>36</u>	<u>36</u>
Total of Bank bonds			\$	6,233	6,036
				=====	=====

⁽¹⁾ Interest payments on a monthly basis

⁽²⁾ Interest payments on a semi-annual basis

⁽³⁾ Structured Bank bonds referred to exchange rate
bp - basis points

(22) Due to banks and other institutions-

At December 31, 2014 and 2013, due to banks and other institutions are analyzed in the following page.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

	2014		2013	
	Term		Term	
	<u>Short</u>	<u>Long</u>	<u>Short</u>	<u>Long</u>
Pesos:				
Central Bank	\$ 1,232	-	-	-
Multiple bank (on demand)	13,765	-	2,900	-
Development bank ⁽¹⁾	4,892	-	3,309	-
Promotion funds ⁽¹⁾	<u>3,906</u>	<u>1,579</u>	<u>4,187</u>	<u>1,703</u>
	<u>23,795</u>	<u>1,579</u>	<u>10,396</u>	<u>1,703</u>
Foreign currency translated into pesos:				
Commercial bank ⁽²⁾	12,975	-	7,548	-
Development bank ⁽¹⁾	1,567	-	15	7
Promotion funds ⁽¹⁾	<u>1,516</u>	<u>589</u>	<u>407</u>	<u>434</u>
	<u>16,058</u>	<u>589</u>	<u>7,970</u>	<u>441</u>
Total by term	<u>39,853</u>	<u>2,168</u>	<u>18,366</u>	<u>2,144</u>
Total due to Banks and other institutions	\$ 42,021		20,510	
	=====		=====	

⁽¹⁾ Funds granted under the development fund program (refer to note 12c).⁽²⁾ Resources from related parties.

At December 31, 2014 and 2013, the annual average rates (unaudited) are analyzed as follows:

	<u>Pesos</u>		<u>Foreing currency</u>	
	<u>2014</u>	<u>2013</u>	<u>2014</u>	<u>2013</u>
Development bank	4.62%	5.46%	3.52%	3.11%
Promotion funds	3.67%	3.83%	1.24%	1.21%

(23) Technical reserves-

At December 31, 2014 and 2013, the technical reserves are shown in the following page.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

		<u>2014</u>	<u>2013</u>
Current risk:			
Life	\$	11,253	10,506
Accidents and sickness		<u>11</u>	<u>11</u>
		<u>11,264</u>	<u>10,517</u>
Contractual obligations:			
Claims and maturities		291	259
Claims occurred and not reported		339	321
Dividends on policies		-	1
Deposited premiums		<u>37</u>	<u>14</u>
		<u>667</u>	<u>595</u>
Estimated:			
Contingencies		161	160
Special		<u>161</u>	<u>160</u>
		<u>322</u>	<u>320</u>
Total technical reserves	\$	12,253	11,432
		=====	=====

For the years ended December 31, 2014 and 2013, the charge to income for the net increase in technical reserves was \$702 and \$890, respectively.

(24) Employee benefits-

The Group maintains a defined pension plan that covers all employees who reach 60 years old with 5 years of service or 55 years old with 35 years of service. The benefits are based on years of service and the employee's compensation. The Group paid annual contributions to the plan equal to the maximum amount that can be deducted for income tax purposes based on the projected unit credit method.

In addition to the defined benefit pension plan, the Group sponsors other postretirement benefits through pantry vouchers, life insurance and major medical plan that provide postretirement medical benefits to employees who have rendered their services to the Group until their retirement date and for their wife, parents and child under 21 years.

Moreover, the Group grants short-term benefits such as paid vacations, vacation premiums, savings fund, year-end bonus, etc.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

Effective April 2004, the defined contribution component was included in the pension plan and starting 2007, in the postretirement medical benefits plan. At present, only unionized workers who were hired before the implementation of the define contribution component and those workers who expressed their intention to continue under the defined contribution component participate in the defined pension plan and in the postretirement benefits. The remaining employees elected to move to the defined contribution pension plan and the defined contribution postretirement medical benefits plan.

In addition to the defined benefit pension plan, the post-retirement benefit pension plan and the defined contribution pension plan, the Group pays the benefits provided by the Federal Labor Law in relation to the legal severance payment for reasons other than restructuring, as well as seniority premium. The latter is paid in the event of death, invalidity, resignation after fifteen years of service and severance payment for reasons other than restructuring and retirement.

The amounts for short-term benefits payable at December 31, 2014 amounted to \$1,367 (\$1,362 in 2013), and are recorded under the caption "Sundry creditors and other accounts payable" in the consolidated balance sheet.

Cash flows-

Contributions and benefits paid were as follows:

		Funds		Paid benefits	
		<u>contributions</u>		<u>2014</u>	<u>2013</u>
		<u>2014</u>	<u>2013</u>		
Termination	\$	19	26	32	26
Retirement		120	315	181	167
Other post retirement benefits		<u>83</u>	<u>236</u>	<u>230</u>	<u>217</u>
	\$	222	577	443	410
		===	===	===	===

The cost, obligations and other pension plans, seniority premiums and fees at the end of the employment relationship other than restructuring, referred to in note 3(x) were determined based on estimates prepared by independent actuaries at December 31, 2014 and 2013. The components of net cost of the years ended December 31, 2014 and 2013 are shown in the following page.

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GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

	Benefits					
	2014			2013		
	<u>Termination</u>	<u>Retirement</u>	<u>Total</u>	<u>Termination</u>	<u>Retirement</u>	<u>Total</u>
Net periodic (income) cost:						
Service cost	\$ 70	17	87	69	63	132
Financial cost	33	176	209	28	152	180
Return on plan assets	(2)	(92)	(94)	(2)	(90)	(92)
Net actuarial gain or loss	(49)	58	9	(83)	59	(24)
Labour cost of past services:						
Amortization of prior services and plan amendments	-	15	15	-	15	15
Effect from early settlement prior to early extinction	<u>3</u>	<u>24</u>	<u>27</u>	<u>-</u>	<u>(16)</u>	<u>(16)</u>
Net period cost	\$ 55	198	253	12	183	195
	==	===	===	==	===	===

	Other Post-retirement benefits	
	2014	2013
	<u>2014</u>	<u>2013</u>
Net periodic (income) cost:		
Service cost	\$ 39	51
Financial cost	216	202
Return of plan assets	(172)	(177)
Net actuarial gain or loss	92	108
Effect from early settlement prior to early extinction	<u>-</u>	<u>(3)</u>
Net period cost	\$ 175	181
	====	====

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

Below is the determination of liabilities for benefit plans at December 31, 2014 and 2013.

2014

	<u>Retirement benefits</u>		Other	
	<u>Seniority</u>	<u>Pension</u>	Post-	
	<u>Premium</u>	<u>Plan</u>	retirement	<u>Total</u>
			<u>Benefits</u>	
Defined benefit obligation:				
Defined benefit obligation at beginning of the year	\$ 47	2,501	3,082	5,630
Service cost	4	14	39	57
Interest cost	3	173	216	392
Actuarial gain or loss	3	114	279	396
Paid benefits	(4)	(177)	(230)	(411)
Reduction/liquidation effect	<u>(1)</u>	<u>(70)</u>	<u>(34)</u>	<u>(105)</u>
Defined benefit obligation at end of the year	\$ 52	2,555	3,352	5,959
	==	=====	=====	=====

2013

	<u>Retirement benefits</u>		Other	
	<u>Seniority</u>	<u>Pension</u>	Post-	
	<u>Premium</u>	<u>Plan</u>	retirement	<u>Total</u>
			<u>Benefits</u>	
Defined benefit obligation:				
Defined benefit obligation at beginning of the year	\$ 52	2,617	3,533	6,202
Service cost	4	59	51	114
Interest cost	3	149	201	353
Actuarial gain or loss	(9)	(55)	(417)	(481)
Paid benefits	(3)	(164)	(217)	(384)
Reduction/liquidation effect	<u>-</u>	<u>(105)</u>	<u>(69)</u>	<u>(174)</u>
Defined benefit obligation at end of the year	\$ 47	2,501	3,082	5,630
	==	=====	=====	=====

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

Below is the determination of plan benefits assets as of December 31, 2014 and 2013:

	Retirement benefit		Other	
	Seniority	Pension	Post-	
	premium	Plan	retirement	Total
			benefits	
<u>2014</u>				
Plan assets:				
Plan assets at the beginning of the year	\$ (44)	(1,345)	(2,486)	(3,875)
Expected performance	(3)	(89)	(172)	(264)
Actuarial gain or loss	(1)	(27)	(53)	(81)
Bank contributions	(3)	(117)	(83)	(203)
Paid benefits	4	177	230	411
Anticipated liquidations	<u>-</u>	<u>58</u>	<u>18</u>	<u>76</u>
Plan assets	\$ (47)	(1,343)	(2,546)	(3,936)
	==	=====	=====	=====
<u>2013</u>				
Plan assets:				
Plan assets at the beginning of the year	\$ (38)	(1,209)	(2,465)	(3,712)
Expected performance	(3)	(87)	(177)	(267)
Actuarial gain or loss	2	67	146	215
Company contributions	(8)	(307)	(236)	(551)
Paid benefits	3	164	217	384
Anticipated liquidations	<u>-</u>	<u>27</u>	<u>29</u>	<u>56</u>
Plan assets	\$ (44)	(1,345)	(2,486)	(3,875)
	==	=====	=====	=====

The Group estimates that during 2015 they will make contributions to defined benefit plans amounting to \$230 (includes termination seniority premium).

Below are the categories of plan assets at December 31, 2014 and 2013:

	Retirement benefit		Other
	Seniority	Pension	Post-
	premium	plan	retirement
			benefits
<u>2014</u>			
Fair value of the plan assets:			
Local equity instruments	25%	22%	22%
Global equity instruments	13%	11%	11%
Debt instruments (nominal rate)	28%	38%	36%
Debt instrument (real rate)	30%	26%	27%
Short term debt instruments	<u>4%</u>	<u>3%</u>	<u>4%</u>
Total	100%	100%	100%
	=====	=====	=====

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

<u>2013</u>	<u>Retirement benefit</u>		<u>Other</u>
	<u>Seniority premium</u>	<u>Pension plan</u>	<u>Post-Retirement benefits</u>
<u>Fair value of the plan assets:</u>			
Local equity instruments	20%	20%	21%
Global equity instruments	9%	10%	10%
Debt instruments (nominal rate)	31%	32%	33%
Debt instruments (real rate)	33%	31%	35%
Short term debt instruments	<u>7%</u>	<u>7%</u>	<u>1%</u>
Total	100%	100%	100%
	=====	=====	=====

The expected long-term return rate of the assets depends on the mix of the investment fund, while the information on the investment policy and the expected and current return depend on the portfolio assets.

According to the current Group investment policy, the expected return of the assets is obtained as follows:

	<u>Asset distribution(1)</u>	<u>Expected return (2)</u>	<u>Total (1) x (2)</u>
Local equity instruments	20.0%	10.70%	2.14%
Global equity instruments	10.0%	8.70%	0.87%
Debt instruments (nominal rate)	<u>70.0%</u>	5.66%	<u>3.96%</u>
Total	100.0%		6.97%
	=====		=====

Below are the amounts of the last four preceding annual periods of the defined benefit obligation, fair value of plan assets, the status of the plan and the experience adjustments arising from the liabilities and assets of the plan.

	<u>Seniority Premium</u>				
	<u>2014</u>	<u>2013</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Defined benefit liabilities	\$ 52	47	52	39	37
Plan assets	<u>(47)</u>	<u>(44)</u>	<u>(38)</u>	<u>(32)</u>	<u>(24)</u>
Plan situation	5	3	14	7	13
Actuarial gain (loss):					
Plan liabilities	3	(9)	16	2	5
Plan assets	<u>(1)</u>	<u>2</u>	<u>(2)</u>	<u>(3)</u>	<u>(1)</u>
	==	==	==	==	==

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

Pension plan					
	<u>2014</u>	<u>2013</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Defined benefit liabilities	\$ 2,555	2,501	2,617	2,052	2,209
Plan assets	(1,343)	(1,345)	(1,209)	(1,041)	(1,044)
Plan situation	1,212	1,156	1,408	1,011	1,165
Actuarial gain (loss):					
Plan liabilities	114	(55)	662	40	218
Plan assets	(27)	67	(58)	40	(58)
	====	====	=====	=====	=====
Other post-retirement benefits					
	<u>2014</u>	<u>2013</u>	<u>2012</u>	<u>2011</u>	<u>2010</u>
Defined benefit liabilities	\$ 3,352	3,082	3,533	2,654	2,433
Plan assets	(2,546)	(2,486)	(2,465)	(2,105)	(2,036)
Plan situation	806	596	1,068	549	397
Experience adjustments:					
Plan liabilities	279	(417)	844	311	469
Plan assets	(53)	(146)	(123)	37	(77)
	=====	=====	=====	=====	=====

At December 31, 2014 and 2013 the present value of the liabilities for the benefits of the plans are as follows:

		Benefits				Other post-retirement benefits	
		Termination		Retirement			
		2014	2013	2014	2013	2014	2013
Obligations for bested benefits	\$	525	501	1,803	1,744	2,632	2,997
		===	===	=====	=====	=====	=====

		Benefits				Other post-retirement benefits	
		Termination		Retirement			
		2014	2013	2014	2013	2014	2013
Defined benefit liabilities amount	\$	546	520	2,607	2,548	3,352	3,082
Fair value plan assets		(22)	(33)	(1,390)	(1,389)	(2,546)	(2,486)
Funds financial situation		524	487	1,217	1,159	806	596
Unrecognized past services:							
Plan modifications		-	-	(167)	(187)	-	-
Actuarial (loss) / gain		-	-	(1,190)	(1,191)	(1,586)	(1,468)
Projected Liabilities / (Assets)	\$	524	487	(140)	(219)	(780)	(872)
		===	===	=====	=====	=====	=====

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

	<u>Termination and retirement benefits</u>		<u>Other post-retirement benefits</u>	
	<u>2014</u>	<u>2013</u>	<u>2014</u>	<u>2013</u>
Nominal discount rate used to show the present value of obligations	6.75%	7.25%	6.75%	7.25%
Nominal rate of increase in the levels of future salaries	4.75%	4.75%	4.75%	4.75%
Nominal rate of return expected in the plan assets	7.00%	7.25%	7.00%	7.25%
Medical inflation rate	-	-	6.75%	6.75%
Average remaining work life of employees (applicable to retirement benefits)	13.31	16.06	13.14	12.62

At December 31, 2014 and 2013, the amortization periods in years of the remaining items are shown as follows:

	<u>Retirement benefits</u>		<u>Other post-retirement benefits</u>
	<u>Seniority Premium</u>	<u>Pension plan</u>	
<u>2014</u>			
Plan modifications	-	12 years	-
Actuarial (loss) / gain	18 years	13 years	13 years

	<u>Retirement benefits</u>		<u>Other post-retirement benefits</u>
	<u>Seniority Premium</u>	<u>Pension plan</u>	
<u>2013</u>			
Plan modifications	-	13 years	-
Actuarial (loss) / gain	17 years	16 years	13 years

The effect of the increase or decrease of one percentage point in the increase rate of medical expenses used in the actuarial projections is shown below:

	<u>Increase in 1%</u>	<u>Decrease in 1%</u>
Labour cost plus financial cost	\$ 31	(25)
Defined benefit obligations	372	(294)
	=====	=====

For the years ended at December 31, 2014 and 2013, the Group recognized expenses for defined contribution plans, which amount to \$134 and \$187, respectively.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos, except otherwise indicated)

(25) Share based payments-

At December 31, 2014 and 2013, the amount of outstanding share based payment awards amounted to \$194 and \$241, respectively, and were registered in the caption “Sundry creditors and other accounts payable”. The cost of these programmes for the years ended December 31, 2014 and 2013 of \$55 and \$132 respectively, was included within “Administrative and promotional expenses” in the consolidated income statement. Payments made during the years 2014 and 2013 were \$102 and \$200, respectively.

(26) Subordinated debt issued-

At December 31, 2014 and 2013, the subordinated debentures in pesos and foreign currency convertibles and non convertibles into shares of its capital stock. The debentures and accrued interest thereon are analyzed as follows:

	<u>2014</u>	<u>2013</u>
<u>Debentures issued:</u>		
In 2008, maturing in 2018 ⁽¹⁾	\$ 4,090	4,090
In 2009, maturing in 2019 ⁽²⁾	4,421	3,924
In 2013, maturing in 2022 ⁽³⁾	1,621	1,439
Accrued interest	<u>12</u>	<u>10</u>
Total subordinated debentures	\$ 10,144 =====	9,463 =====

⁽¹⁾ During October and December 2008, the Group made two public offerings of subordinated debt obligations, non convertible to HSBC shares for a total amount of \$1,818 and \$2,300, respectively. Of the second issuance, as of December 31, 2014 and 2013, \$28, had not been placed. The subordinated obligations have a maturity of 10 years and bear interest at a rate equivalent to the 28-day TIIE plus 60 and 200 basis points, respectively.

⁽²⁾ As part of a programme of subordinated non convertible debt issuance (both preference and non preference securities), authorised by the Banking Commission, the Group undertook a foreign currency issuance on 26 June 2009. This issuance was for a total of US\$300 million, of which US\$196.7 million was placed on the date of issue and the remaining US\$103.3 million was placed at a later date. The term of this issuance is 10 years and it pays a variable rate of interest at Libor plus 3.5 basis points.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

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(Millions of pesos)

- ⁽³⁾ On January 31, 2013, the Bank issued foreign currency preferred subordinated debentures subject to mandatory conversion into common shares representing capital stock, provided that any of the following conditions is met: (i) where the result from dividing the Tier 1 Basic Capital (note 28d) by the Bank's total weighted assets subject to risk is 4.5% or less; or (ii) where the Banking Commission notifies the Bank that it has not complied with the minimum remedial action in case of not having the minimum capitalization level required or when non complying with the minimum capitalization index required by the Credit Institution Law (LIC for its acronym in Spanish language) and the Bank does not rectify such situation. Such issuance totaled US\$110 million, was totally subscribed, has a 10 year maturity and bears interest at the 30-day LIBOR rate plus 3.65 basis points. Such issuance was recorded as a liability, considering the aforementioned conversion conditions, the Bank's capitalization index and financial condition at the date of issuance of the financial statements.

At December 31, 2014 and 2013, the balance of subordinated obligations count as supplementary capital for the determination of the capitalization ratio, which is calculated based on the applicable rules as of those dates, issued by the Central Bank.

(27) Income Tax (IT) and employee statutory profit sharing (ESPS)-

On December 11, 2013, a decree was published in the Official Gazette whereby several tax provisions were amended, supplemented, and repealed. This decree became effective as of January 1, 2014. Such decree repeals the Single Rate Business Tax law (IETU for its acronym in Spanish language), the Cash Deposits (IDE) Law and the IT Law in effect through December 31, 2013 and a new IT Law is issued.

a) Income tax

At December 31, 2014 and 2013, the IT expense shown in the consolidated statement of income is analyzed as follows:

	<u>2014</u>	<u>2013</u>
IT expenses from the Group as individual entity	\$ -	-
IT expenses from Bank and subsidiaries at the rate 30%	1,376	2,381
IT expenses from Bank and subsidiaries at the rate 30% from past years	(371)	(151)
IETU of subsidiaries	<u>-</u>	<u>14</u>
Income tax in the consolidated statement of income	\$ 1,005 =====	2,244 =====

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(Millions of pesos)

Under the tax legislation in effect in 2013, companies paid the greater of their IT or IETU. If IETU was payable, the payment was considered final; i.e. not subject to recovery in subsequent years.

According to the IT Law in effect as of December 31, 2013, the IT and IETU rate for fiscal year 2013 was 30% and 17.5% respectively. The current IT law with effect on January 1, 2014 imposes an IT rate of 30% for 2014 and thereafter.

Deferred IT:

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment.

Deferred IT changes for the years ended December 31, 2014 and 2013, are analyzed as follows:

	<u>2014</u>	<u>2013</u>
Balance at beginning of year	\$ 7,710	6,226
Charged to results:		
IT benefit	735	1,067
Reported in capital:		
Valuation effects of available for sale and derivatives	(129)	255
Effect in capital for the change in the consumer loan methodology	9	240
Others	<u>-</u>	<u>(78)</u>
	\$ <u>8,325</u>	<u>7,710</u>
	=====	=====

The items that give rise to significant portions of the deferred tax assets and liabilities at December 31, 2014 and 2013, are shown in the following page.

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(Millions of pesos)

		<u>2014</u>	<u>2013</u>
Deferred tax assets:			
Allowances:			
Allowance for loan losses	\$	7,460	6,705
Allowance for foreclosed assets		266	277
Other provisions		556	1,129
Non recoverable		-	38
Property, furniture and equipment		730	641
ESPS provision		91	122
Valuation of financial instruments		471	272
Commissions received in advance		231	354
Other		<u>95</u>	<u>30</u>
		<u>9,900</u>	<u>9,568</u>
Deferred tax liabilities:			
Interest from Special CETES UDIS			
Central Bank		(1,039)	(990)
Deferred IT due to deferred ESPS		(115)	-
Valuation of financial instruments		(310)	(233)
Deductions in advance		(111)	(632)
Others		<u>-</u>	<u>(3)</u>
		<u>(1,575)</u>	<u>(1,858)</u>
Net deferred tax asset	\$	<u>8,325</u>	<u>7,710</u>
		=====	=====

Reconciliation of the statutory income tax rate and the effective income tax rate is as follows:

	<u>2014</u>		<u>2013</u>	
	<u>Amount</u>	<u>%</u>	<u>Amount</u>	<u>%</u>
Income before income taxes	\$ 2,365	100%	\$ 4,706	100%
	=====	=====	=====	=====
Expected tax expense	\$ 709	30%	1,411	30%
(Reduction) increase resulting from:				
Inflation effect	(459)	(19%)	(460)	(10%)
Non-deductible expenses	498	21%	356	8%
Tax income on derivatives	(171)	(7%)	(18)	(1%)
Non-taxable interests	(292)	(12%)	(295)	(7%)
Subsidiaries' IETU	-	-	14	1%
Tax SPE	-	-	221	5%
Changed in rates	-	-	(307)	(7%)
Others	<u>(15)</u>	<u>(1%)</u>	<u>255</u>	<u>5%</u>
IT expense	\$ 270	12%	\$ 1,177	24%
	=====	=====	=====	=====

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

Deferred ESPS

From 2014, the base for computing ESPS shall be the taxable income for IT purposes in accordance with article 9 of the IT Law, which amounts to \$287 for the year ended December 31, 2014. The current ESPS rate is 10%.

ESPS income and expense deferred in the statement of income and in the stockholders' equity amounted to \$430 and \$47, respectively.

The effects of ESPS for temporary differences resulting in significant portions of deferred ESPS assets and liabilities as of December 31, 2014, are as follows:

	<u>2014</u>
Deferred Asset:	
Allowance:	
For loan losses	\$ 251
Deduction in advance	54
For various provisions	31
Property, furniture and equipment	23
Valuation of financial instruments	64
Commissions received in advance	5
Others	<u>2</u>
Total deferred asset	<u>430</u>
Deferred liabilities:	
For write-offs of foreclosed asstes	(4)
Interest from Special CETES UDIS	
Central Bank	(15)
Valuation of financial instruments	<u>(26)</u>
Total deferred liabilities	<u>(45)</u>
Net, Deferred Asset	\$ 385
	===

Until December 31, 2013, the Group computed the ESPS considering a limit of one month of salary provided by section III of article 127 of the Federal Labor Law. This amounted to \$398, and was recognized under the caption of "Administrative and promotion expenses" in the consolidated statement of income.

Other considerations:

In accordance with Mexican tax law, the tax authorities are entitled to examine transactions carried out during the five years prior to the most recent income tax return filed.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

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In accordance with the Income Tax Law, companies carrying out transactions with related parties are subject to certain requirements as to the determination of prices, since such prices must be similar to those that would be used in arm's-length transactions.

At December 31, 2014 the balances of the Capital Contributions account of the Group as an standalone entity amount to \$63,928 and at December 31, 2013 amount to \$53,942, on the other hand, with regards to the Previously Tax Retained Earnings (CUFIN) and since some changes were made to the tax legislation in effect during 2014, the Income Tax Law provides an additional withholding for the payment of dividends for income arising from 2014, applicable to Individuals and Nonresidents. It also provides that taxpayers will have CUFIN on income generated as of December 31, 2013 (updated balance of \$1,693) and there is no CUFIN on income generated from January 1, 2014.

(28) Stockholders' equity-

The main features of the accounts comprising stockholders' equity are the following:

(a) *Structure of capital stock -*

Movements in 2014

At Extraordinary General Stockholders' Meeting held on April 28, 2014, a resolution was passed to apply the net income for the year 2013 of \$3,714 as follows: \$186 to capital reserves and \$3,528 to prior years' income (loss), which will be made available to the stockholders when the Board of Directors will so decide it.

At Extraordinary General Stockholders' Meeting held on March 21, 2014, a resolution was passed for the distribution of a dividend, which was paid on March 28, 2014 at the rate of \$1.3415 pesos per share for each of the 2,818,383,598 outstanding shares, for a total payment of \$3,781, which was charged to prior years' income (loss) and paid out from the previously taxed retained earnings.

At December 31, 2014 and 2013, capital stock is represented by 2,818,383,598 subscribed and paid up shares, of which 2,813,547,652 shares are represented by Series "F" shares and 4,835,946 Series "B" shares, with a par value of two pesos each.

Movements in 2013

On April 26, 2013, the General Ordinary Stockholders' Meeting agreed to apply the net income for the year 2012 of \$6,016 as follows: \$301 to capital reserves and \$5,715 to retained earnings.

At the Board of Directors meeting on March 21, 2013, the Board of Director authorized a maximum dividend of \$2,500, equivalent to a price per share of \$0.8870 pesos for each one of the outstanding without coupon, with charge to retained earnings account. This dividend was paid on March 26, 2013.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

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On January 24, 2013, the General Extraordinary Stockholders' Meeting agreed to increase the contributed capital in \$5,150 by issuing 263'032,564 shares with a par value of two pesos each, corresponding 262,581,237 to Series "F" and 451,237 to Series "B", which were paid at a price of \$19.5793 pesos per share; therefore, the difference with respect to the par value was recorded as additional paid-in capital.

The share capital at December 31, 2013 is integrated by \$5,637 (nominal) integrated by 2,813,547,652 shares of series "F" and 4,835,946 shares of series "B" with nominal value of two pesos each, which are fully subscribed and paid.

(b) Comprehensive income-

The comprehensive income reported in the consolidated statement of changes in stockholders' equity represents the results of the Group's activities during the year and includes the net income, the gain or loss from mark to market of investments in "Available-for-sale" securities and for cash flow hedges, and additionally for the constitution of allowance for loan losses derived of a change in the calculation methodology (note 4 and 3(1)).

(c) Restrictions on stockholders' equity-

The Credit Institutions Law requires that the Group segregate 10% of its net income for the year to the statutory reserves up to the amount of its paid-in capital stock.

Stockholder contributions may be reimbursed to the stockholders tax-free, to the extent that the tax basis of such contributions equal or exceed stockholders' equity.

The un-appropriated retained earnings of subsidiaries may not be distributed to the Group's stockholders until these are received by way of dividends. Also, gains from marking to market investment securities and derivative transactions may not be distributed until realized.

(d) Capitalization (unaudited)-

In accordance with the Law of Credit Institutions, credit institutions are required to maintain a net capital in relation to their exposure to market risk, credit risk and other risks which are incurred during the course of their operations. Net capital cannot be lower than the total of adding up the capital requirement for each type of risk. In accordance with the Capitalization Rules, credit institutions must comply with the capital requirement for operational risk.

Information in relation to the Bank's net capital, risk based assets and capital requirements as of December 31, 2014 and 2013, is shown on the following page. The amounts for 2014 are in process of validation by the Central Bank. The amount for 2013 correspond to those Published by the Central Bank at the date of issuance of the Bank's consolidated financial statements.

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GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

	<u>2014</u>	<u>2013</u>
<u>Basic, supplementary and net capital</u>		
Stockholders' equity	\$ 48,048	47,555
Reduced by:		
Intangible assets	(6,227)	(5,575)
Investments in shares of financial entities	(45)	(17)
Investments in shares of entities	(79)	-
Investment in subordinated debt	<u>(104)</u>	<u>(92)</u>
Basic capital (Tier 1)	<u>41,593</u>	<u>41,871</u>
Add:		
Not convertible subordinated debt	6,384	7,182
Subordinated debt eligible for conversion	1,622	1,439
General allowance for loan losses	<u>1,233</u>	<u>1,287</u>
Supplementary capital (Tier 2)	<u>9,239</u>	<u>9,908</u>
Net capital (Tier 1+ Tier 2)	\$ <u>50,832</u> =====	<u>51,779</u> =====

On November 28, 2012 was a published in the DOF "resolution amending the general Dispositions applicable to credit institutions" (Resolution). This resolution is intended to strengthen the composition of the net capital of credit institutions consistent with the most recent international consensus in this field in accordance with the guidelines established by the Capital Agreement issued by the Committee of Banking Supervision (Basel III).

The resolution entries into force on January 1, 2013, except as provided in articles transient thereof, which stipulate the entry into force of certain provisions at a later date.

Intangibles assets.- Consider excess deferred taxes on the 10% capacity as the Basic Capital deduction required by \$3,983 and \$3,048 to December 31, 2014 and 2013, respectively.

Non-convertible subordinated debentures - According to the Provisions, the supplementary capital shall be computed based on the amount as of December 31, 2012, which was \$7,980, 80% (\$6,384) and 90% (\$7,182) for December 31, 2014 and 2013, respectively, plus 100% corresponding to the issuance of January 31, 2013, which meets with the requirements of exhibit 1-S.

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Risk-based assets and capital requirements

	Equivalent Risk weighted assetss		Capital Requirement	
	<u>2014</u>	<u>2013</u>	<u>2014</u>	<u>2013</u>
<i>Market risk:</i>				
Transactions or positions:				
In pesos at nominal rates	\$ 83,436	66,526	6,675	5,322
In pesos at interest rate over nominal rate	274	910	22	73
In pesos at interest rates or denominated in UDIS	1,382	1,222	111	98
In foreign currency at nominal rates	8,420	6,503	673	520
In UDIS or with yields linked to the Consumer Price Index	21	9	2	1
Foreign currency positions or with Exchange rate indexed yields	625	679	50	54
Share transactions or transaction based on shares	<u>1</u>	<u>33</u>	<u>-</u>	<u>3</u>
Total market risk to the following page	\$ 94,159 =====	75,882 =====	7,533 =====	6,071 =====
<i>Credit risk:</i>				
Group II (weighted at 20%)	\$ 277	6	22	-
Group II (weighted at 50%)	5,382	7,713	431	617
Group III (weighted at 10%)	10	36	1	3
Group III (weighted at 11.5%)	489	401	39	32
Group III (weighted at 20%)	4,813	3,960	385	317
Group III (weighted at 23%)	74	129	6	10
Group III (weighted at 100%)	268	464	21	37
Group IV (weighted at 20%)	5,665	3,239	453	259
Group V (weighted at 20%)	604	499	48	40
Group V (weighted at 50%)	1,716	1,680	137	134
Group V (weighted at 150%)	7,578	5,694	606	456
Group VI (weighted at 50%)	6,270	5,203	502	416
Group VI (weighted at 75%)	3,361	3,446	269	276
Group VI (weighted at 100%)	42,015	43,798	3,361	3,503
Group VII (weighted at 10%)	581	432	47	35
Group VII (weighted at 20%)	8,316	5,180	665	414
Group VII (weighted at 23%)	9,655	6,481	772	519
Group VII (weighted at 50%)	<u>987</u>	<u>673</u>	<u>79</u>	<u>54</u>
Credit risk to the following page	\$ <u>98,061</u>	<u>89,034</u>	<u>7,844</u>	<u>7,122</u>

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GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

	Equivalent risk weighted assets		Capital requirement	
	<u>2014</u>	<u>2013</u>	<u>2014</u>	<u>2013</u>
Credit risk from previous page	\$ 98,061	89,034	7,844	7,122
Group VII (weighted at 100%)	117,234	106,939	9,379	8,556
Group VII (weighted at 115%)	500	267	40	21
Group VII (weighted at 150%)	-	646	-	52
Group VIII (weighted at 125%)	8,064	8,488	645	679
Group X (weighted at 1,250%)	158	998	13	80
Others assets (weighted at 100)	19,995	23,429	1,600	1,874
Securitizations (weighted at 20%)	49	151	4	12
Securitizations (weighted at 50%)	2	10	-	1
Securitizations (weighted at 1,250%)	351	370	28	30
Resecuritizations (weighted at 1,250%)	<u>1,832</u>	<u>2,270</u>	<u>147</u>	<u>182</u>
Total credit risk	246,246	232,602	19,700	18,609
Total Operational risk	44,250	41,097	3,540	3,287
Total market risk from previous page	<u>94,159</u>	<u>75,882</u>	<u>7,533</u>	<u>6,071</u>
Total market credit and operational risk	\$ <u>384,655</u>	<u>349,581</u>	<u>30,773</u>	<u>27,967</u>
	=====	=====	=====	=====

Capitalization ratios:

	<u>2014</u>	<u>2013</u>
Capital to credit risk assets:		
Basic capital (Tier 1)	16.89%	18.00%
Supplementary capital (Tier 2)	3.75%	4.26%
Net capital (Tier 1 + Tier 2)	20.65%	22.26%
Capital to market, credit and operational risks assets:		
Basic capital (Tier 1)	10.81%	11.98%
Supplementary capital (Tier 2)	2.40%	2.83%
Net capital (Tier 1 + Tier 2)	13.22%	14.81%

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

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As discussed in note 4, since June 2013 the Group opted for calculating preventive reserves by considering the expected loss methodology issued by the authority pursuant to the Provisions, except for the credits granted to financial entities for which the beginning application was in March 2014, which had an effect on the Credit Risk and the Supplementary Capital. For Supplementary Capital computed at December 31, 2014 and 2013, the difference is considered between the total Reserves created for Investment Projects, Financial Entities and Other additional reserves and the reserves for expected losses and additional reserves not considered Supplementary Capital.

The Bank reports on a monthly basis the trend of the capitalization indices, detailing basic capital and net capital to the Risk Committee and the Assets and Liabilities Committee. In addition, significant variances in the risk-weighted assets by credit and market risk, and variances in stockholders' equity, are explained and reported.

In addition, prior to undertaking any material commercial banking or treasury transactions, an assessment is made to determine their effect on the capital requirement. Based on this, the above mentioned Committees may authorize the proposed transactions. For these operations the Bank considers as a basis the minimum capitalization index, which is higher than the required by the Banking Commission in the Early Warnings.

(29) Related party transactions and balances-

During the normal course of business, the Group carries out transactions with related parties. According to the Group's policies, the Board of Directors authorizes all credit transactions with related parties, which are granted at market rates with guarantees and terms in accordance with sound banking practices. At December 31, 2014, the Group had granted loans to related parties totalling \$1,737 (\$318 in 2013).

During the years in 2014 and 2013, the Group maintained derivative liability positions with related parties, which amounted to \$9,134 and \$2,875, respectively.

The main transactions carried out with related parties during the years ended December 31, 2014 and 2013, are shown as follows:

		<u>2014</u>	<u>2013</u>
<u>Transactions:</u>			
Income:			
Administrative services	\$	1,191	1,105
		=====	=====
Expenses:			
Interest and commissions, paid	\$	83	-
Administrative expenses		1,058	989
		=====	=====

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

Balances receivable from and payable to related parties as of December 31, 2014 and 2013, were as shown as follows:

	2014		2013	
	<u>Receivable</u>	<u>Payable</u>	<u>Receivable</u>	<u>Payable</u>
HSBC Latin America Holdings (UK) Limited	\$ -	7	266	5
HSBC Global Asset Management (USA) Inc.	-	3	-	3
HSBC Bank Brasil, S. A. Banco multiplo	174	200	239	162
HSBC Holdings Plc	100	474	54	123
HSBC Colombia, S. A.*	-	-	15	-
HSBC Bank USA National Association	-	19	-	8
HSBC Software Development (Guangdong)	-	4	-	3
HSBC New York Life Seguros de Vida (Argentina), S. A.	16	-	8	-
HSBC Bank Argentina, S. A.	43	11	44	20
HSBC Argentina Holding, S. A.	9	-	6	2
HSBC Private Bank (SUISSE), S. A.	1	-	1	10
HSBC Bank Uruguay, S. A.	9	-	3	-
HSBC Bank Canada, S. A.	-	12	-	3
HSBC Bank Chile, S. A.	4	-	5	-
HSBC Bank Plc UK	12	142	11	67
The Hong Kong and Shanghai Banking Corporation Limited	-	96	-	30
HSBC Software Development (India) Private Limited	-	53	-	26
HSBC Software Development (Brazil)	-	16	-	1
HSBC Technologies and Services (USA) Inc.	-	88	-	13
HSBC France	-	7	-	3
HSBC Global Operations Company Limited (before HSBC Global Resourcing (UK) Limited)	-	-	-	42
HSBC Insurance Holdings Limited	-	12	-	7
HSBC Securities (USA) Inc	11	367	39	19
HSBC Bank Middle East Limited	-	-	-	1
HSBC Global Operations Company Limited	-	30	-	-
HSBC PB Service (SUISSE), S. A.	-	-	-	5
Total related parties	\$ 379	1,541	691	553
	===	=====	===	===

(*) As of December 31, 2014, these entities are no longer considered as related parties.

Accounts receivable and payable from with to related parties do not generate interest and do not have defined maturity.

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GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

(30) Memorandum accounts-**(a) Irrevocable lines of credit and guarantees-**

At December 31, 2014, the Bank had irrevocable commitments arising from issuance of letters of credit, where, through loans, the Group ensured paying customers to third parties irrevocable commitments amounted to \$33,874 (\$25,561 in 2013).

At December 31, 2014, the Group had no provisions for letters of credit and guarantee receivables included in the allowance for loan losses (\$29 in 2013).

At December 31, 2014 and 2013, the Group had no losses caused by the guarantee and letters of credit.

(b) Assets in trust or under mandate-

At December 31, 2014 and 2013, the Group's trust activity, which is recorded in memorandum accounts, is summarized as follows:

	<u>2014</u>	<u>2013</u>
Type of trust:		
Administrative	\$ 321,151	298,141
Guarantee	51,494	56,296
Investment	52,901	52,811
Other	<u>31,979</u>	<u>31,285</u>
	<u>457,525</u>	<u>438,533</u>
Mandates to:		
Administrative	568	840
Guarantee	70	93
Investment	<u>3</u>	<u>3</u>
	<u>641</u>	<u>936</u>
	\$ 458,166	439,469
	=====	=====

Trust activities revenue for the years ended December 31, 2014 and 2013 amounted to \$171 and \$180, respectively.

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Notes to Consolidated Financial Statements

(Millions of pesos)

(c) Investments on behalf of customers-

At December 31, 2014 and 2013 the Group received funds from the public and invested them in various instruments of the Mexican financial system on behalf of its customers, which are recorded in memorandum accounts as follows:

	<u>2014</u>	<u>2013</u>
Funds of investment companies:		
Managed by the Bank	\$ 3,595	3,091
Government securities	15,672	19,980
Equities and other	20,359	22,924
Other	<u>6,607</u>	<u>4,358</u>
	\$ 46,233	50,353
	=====	=====

In case that the funds are invested in the Group's own instruments, the amounts of such funds are included in the consolidated balance sheet.

(d) Assets in custody-

The Group records in this account the assets and securities of third parties it receives in custody or for management purposes. At December 31, 2014 and 2013, this account comprises:

	<u>2014</u>	<u>2013</u>
Custody	\$ 379,498	289,011
Administration	49,247	49,894
Guarantee	6,920	1,294
Collection	<u>880</u>	<u>1,019</u>
	\$ 436,545	341,218
	=====	=====

For custody operations, the types of goods mainly handled are: stocks and shares in custody, government paper, bankers' acceptances, corporate bonds and shares. Amounts related to securities issued by the institution itself amount to \$3,549 (\$2,885 in 2013) and are classified as follows:

	<u>2014</u>	<u>2013</u>
Bank paper	\$ 3,436	2,773
In private debt	<u>113</u>	<u>112</u>
	\$ 3,549	2,885
	=====	=====

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(Millions of pesos)

For management operations, types of goods, including goods and foreign values that are received for administration are mainly: bank stocks, private or government.

At December 31, 2014 and 2013, income from activity of assets under custody and administration operations amount to \$126 and \$94, respectively.

(31) Additional information on results of operation and segments-

(a) Condensed statements of operations and cash flows by segment-

The condensed consolidated statements of operations and cash flows by segment includes Retail Banking and Wealth Management (RBWM), Commercial Banking (CMB) and Global Banking and Markets (GBM). A brief description of the Group's business segments follows:

Retail Banking and Wealth Management – Focused primarily on individuals that comprise mainly consumer products, which include credit cards, personal and car loans as well as mortgage loans and traditional deposits.

Commercial Banking – Focused primarily on corporations, offering financing in Mexican pesos and other currencies, lines of credit for working capital, term loans, and the financing of exports, in addition to financial services relating to checking and investment accounts and cash management.

Global Banking & Markets – Focused primarily on corporations, which comprise: trust, treasury and custody services, corporate finance advisory, as well as risk management and cash flow services. This segment comprises products such as letters of credit, factoring, discounted documents and investments in the money and capital markets.

The allocation of income to each segment is determined in accordance with the profile of the client. For the allocation of expenses to each segment a cost management system is used which utilizes an Activity Based Costing (ABC / ABM) approach, although directly identifiable segment costs are not subject to this methodology. Within the Bank a catalogue of transactions and their relevant costs exists, and in this way each time that a transaction is completed for a client, the cost of this transaction is registered in the segment to which that client belongs.

In the following page is presented the condensed statements of operations and cash flows by segment for the years ended December 31, 2014 and 2013.

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GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to the Consolidated Financial Statements

Condensed statements of operations by segment

Years ended December 31, 2014 and 2013

(Millions of pesos)

	RBWM		CMB		GBM		Total	
	<u>2014</u>	<u>2013</u>	<u>2014</u>	<u>2013</u>	<u>2014</u>	<u>2013</u>	<u>2014</u>	<u>2013</u>
Financial margin	\$ 14,026	14,968	5,428	5,973	2,502	1,651	21,956	22,592
Allowance for loan losses	<u>(5,621)</u>	<u>(5,963)</u>	<u>(2,116)</u>	<u>(1,525)</u>	<u>(265)</u>	<u>(598)</u>	<u>(8,002)</u>	<u>(8,086)</u>
Adjusted financial margin	8,405	9,005	3,312	4,448	2,237	1,053	13,954	14,506
Commissions and fees, net	4,720	4,752	1,258	1,499	603	658	6,581	6,909
Financial intermediation income	327	247	203	184	1,060	1,989	1,590	2,420
Other operating income	1,721	2,330	420	480	264	(280)	2,405	2,530
Administrative and promotion expenses	<u>(14,008)</u>	<u>(13,571)</u>	<u>(5,504)</u>	<u>(5,524)</u>	<u>(2,702)</u>	<u>(2,607)</u>	<u>(22,214)</u>	<u>(21,702)</u>
Total operating income	1,165	2,763	(311)	1,087	1,462	813	2,316	4,663
Equity in the results of non consolidated subsidiaries, associated and affiliated companies	<u>30</u>	<u>26</u>	<u>15</u>	<u>13</u>	<u>4</u>	<u>4</u>	<u>49</u>	<u>43</u>
Income before income tax	<u>\$ 1,195</u>	<u>2,789</u>	<u>(296)</u>	<u>1,100</u>	<u>1,466</u>	<u>817</u>	<u>2,365</u>	<u>4,706</u>

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(Millions of pesos)

The condensed statement of cash flows by segment for the years ended December 31, 2014 and 2013 is presented as follows:

	2014			2013		
	<u>RBWM</u>	<u>CMB</u>	<u>GBM</u>	<u>RBWM</u>	<u>CMB</u>	<u>GBM</u>
Net income	\$ 837	(183)	1,327	2,451	752	511
Adjustment for non cash items	3,009	691	419	4,179	1,608	864
Operating activities	(4,362)	(6,384)	(5,389)	(6,946)	(4,213)	(439)
Investment activities	(505)	(230)	(166)	(949)	(480)	(427)
Financing activities	<u>(1,381)</u>	<u>(1,018)</u>	<u>(1,382)</u>	<u>968</u>	<u>714</u>	<u>968</u>
Net decrease of cash and cash equivalents	(2,402)	(7,124)	(5,191)	(297)	(1,619)	1,477
At the beginning of the year	<u>31,515</u>	<u>20,112</u>	<u>3,780</u>	<u>31,811</u>	<u>21,731</u>	<u>2,304</u>
At end of the year	\$ 29,113	12,988	(1,411)	31,514	20,112	3,781
	=====	=====	=====	=====	=====	=====

The assets (loans) and liabilities (deposit funding) identifiable by the different segments at December 31, 2014 and 2013 are analyzed as follows:

	2014			2013		
	<u>RBWM</u>	<u>CMB</u>	<u>GBM</u>	<u>RBWM</u>	<u>CMB</u>	<u>GBM</u>
Assets	\$ 63,970	81,955	72,842	62,821	81,329	48,618
Liabilities	157,187	87,000	54,430	162,347	94,754	30,419
	=====	=====	=====	=====	=====	=====

Financial Margin

The financial margin for the years ended December 31, 2014 and 2013 is analyzed as follows.

	2014	2013		
		<u>Reclassified</u>	<u>Reclassification</u>	<u>*Reported</u>
Interest income:				
Cash	\$ 913	1,296	(105)	1,401
Investment securities	8,610	6,569	(191)	6,760
Interest and premium on securities purchased under agreements to resell	41	565	-	565
Interest from hedging transactions	600	1,130a	1,130	-
Premium income	<u>2,893</u>	<u>3,030</u>	<u>-</u>	<u>3,030</u>
Subtotal interest income to the following page	\$ <u>13,057</u>	<u>12,590</u>	<u>834</u>	<u>11,756</u>

(*) See explanations in the next page.

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Notes to Consolidated Financial Statements

(Millions of pesos)

			2013		
		2014	Reclassified	Reclassification*Reported	
Subtotal interest income from previous page	\$	13,057	12,590	834	11,756
Loan portfolio:					
Commercial loans		6,456	7,142	-	7,142
Financial Institutions		345	266	-	266
Consumer loans		9,627	10,154	-	10,154
Residential mortgages		2,416	2,157	-	2,157
Government entities		1,133	1,347	-	1,347
Initial fees for loan granting		246	210	-	210
Others		<u>15</u>	<u>155</u>	<u>296</u>	<u>(141)</u>
		<u>33,295</u>	<u>34,021</u>	<u>1,130</u>	<u>32,891</u>
Interest expenses, technical reserves and claims:					
Deposit fuding		(1,506)	(1,366)	288	(1,654)
Time deposit		(2,814)	(3,524)	(108)	(3,416)
Due to Banks and other institutions		(542)	(600)	(180)	(420)
Bank bonds interest		(407)	(162)	-	(162)
Interest and premiums on securities purchased under agreements to resell		(2,189)	(1,911)	-	(1,911)
Interest from hedging transactions		(919)	(1,130)	(1,130)	-
Interest by subordinated debt issued		(411)	(521)	-	(521)
Technical reserve increase		(702)	(890)	-	(890)
Claims and others contractual obligations		(1,761)	(1,169)	-	(1,169)
Others		<u>(88)</u>	<u>(156)</u>	<u>-</u>	<u>(156)</u>
		<u>(11,339)</u>	<u>(11,429)</u>	<u>(1,130)</u>	<u>(10,299)</u>
Financial margin	\$	21,956	22,592	-	22,592
		=====	=====	=====	=====

*Some accounts of the financial margin for the year ended December 31, 2013 have been reclassified to conform to the 2014 presentation, aimed to identify income and expense primarily arising from hedge transactions; without modifying the financial margin.

The composition of the financial margin for premium revenues for the years ended December 31, 2014 and 2013 includes the following policies and premiums issued before the consolidation eliminations (unaudited information) as shown in the following page.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

	2014				2013		
	Number of policies	Number of insured persons	Premiums issued		Number of policies	Number of insured persons	Premiums issued
Accidents	284,209	2,380,893	\$ 255	Accidents	301,717	2,390,461	\$ 307
Life	458,407	2,095,524	2,852	Life	462,803	2,331,834	2,959
Casualty	2	2,026,959	23	Casualty	19,858	1,996,900	136
Pensions	<u>13,309</u>	<u>39,588</u>	<u>16</u>	Pensions	<u>13,586</u>	<u>39,858</u>	<u>16</u>
	<u>755,927</u>	<u>6,542,964</u>	<u>\$ 3,146</u>		<u>797,964</u>	<u>6,759,053</u>	<u>\$ 3,418</u>

(b) Financial intermediation income-

For the years ended December 31, 2014 and 2013, the financial intermediation income is analyzed as follows:

	<u>2014</u>	<u>2013</u>
<i>Valuation gain (loss):</i>		
Investment securities	\$ 584	(277)
Trading derivatives	(1,642)	483
Foreign currency exchange and precious metals	<u>297</u>	<u>178</u>
	<u>(761)</u>	<u>384</u>
<i>Purchase/sale gain (loss):</i>		
Investment securities	1,003	196
Securities repurchase/resell agreements and trading derivatives	976	1,038
Foreign currency exchange and precious metals	<u>372</u>	<u>802</u>
	<u>2,351</u>	<u>2,036</u>
Total financial intermediation income	\$ <u>1,590</u>	<u>2,420</u>

(c) Other operating income-

For the years ended December 31, 2014 and 2013, other operating income is analyzed in the following page.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

<u>Income</u>	<u>2014</u>	<u>2013</u>
Recoveries and reimbursements	\$ 1,099	905
Use of infrastructure and reimbursments	1,215	1,137
Gain on sale of properties	20	1
Gain on sale of foreclosed assets	193	122
Loan to employees	132	137
Cancellation of excess of allowance for loan losses (note 12(d))	32	6
Effect securitization	4	-
Others	<u>406</u>	<u>1,245</u>
	<u>3,101</u>	<u>3,553</u>
 <u>Expenses</u>		
Write off*	(377)	(1,023)
Foreclose assets reserve	(25)	-
Loss on sale of properties	(77)	-
Transfer of loan portfolio (note 12f)	(215)	-
Effect securitization	-	-
Others	<u>(2)</u>	<u>-</u>
Other operating income, net	<u>(696)</u>	<u>(1,023)</u>
	\$ 2,405	2,530
	=====	=====

(*) Within the expenses there are fraud losses of \$223 (\$134 in 2013).

(d) Financial Ratios-

The principal ratios of the Banks as of and for the years ended December 31, 2014 and 2013 are analyzed in the following page.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

	<u>2014</u>	<u>2013</u>
Non-performing loans to total loans	5.29%	5.93%
Allowance for loan losses to past-due loan portfolio	103.67%	100.55%
Operating efficiency (<i>administrative and promotional expenses to average total assets</i>)	3.99%	4.33%
ROE (<i>net income to average stockholders' equity</i>)	2.42%	4.75%
ROA (<i>net income to average total assets</i>)	0.18%	0.43%
Liquidity (<i>liquid assets/liquid liabilities</i>)*	105.13%	102.99%
Financial margin after provision for loan losses /average interest earning assets	2.53%	2.86%
Capital index to credit risk assets	20.65%	22.26%
Capital index to market and credit risk	13.22%	14.81%

* *Liquid assets* – Cash and cash equivalents, trading and available-for-sale securities.* *Liquid liabilities* – Demand deposits, demand and short-term bank and other loans.**(e) Coverage indicators (unaudited)-**

	<u>2014</u>	<u>2013</u>
Technical reserve coverage index	109.40%	107.64%
Minimum guarantee capital coverage index	321.43%	215.97%
Minimum paid-up capital requirement index:		
HSBC Seguros, S.A. de C.V.	144.70%	150.17%
HSBC Pensiones, S.A.	102.38%	195.19%
HSBC Vida, S.A. de C.V.	-	486.46%

(f) Development triangle and claims paid (unaudited)-

The table on the following page, shows the results (in pesos) of the development triangle for insurance and bonding claims at December 31, 2014 and 2013.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

DOTAL SB077

MXP

Historical data of development triangle of claims by business and branch.					
Year of claim					
Claim provisions and payments	Previous year (Year t-4)	Previous year (Year t-3)	Previous year (Year t-2)	Previous year (Year t-1)	Previous year (Year t)
	2010	2011	2012	2013	2014
In the same year	550,000	5,084,529	1,052,558	9,551,991	654,588,096
One year later	1,193,763	100,000	9,591,339		-
Two years later	-	1,250,000	47,037,886	-	-
Three years later	850,000	4,700,000	-	-	-
Four years later	972,369	-	-	-	-
	-	-	-	-	-
Total claims estimate	3,566,132	11,134,529	57,681,783	9,551,991	654,588,096
Paid claims	3,016,132	2,350,000	44,550,584	255,098,345	563,809,908
Claim provisions	550,000	8,784,529	13,131,199	- 245,546,354	90,778,188
Earned premium	179,252,927	540,856,005	821,260,233	1,137,621,551	1,350,659,226

VIDA INDIVIDUAL SB077

MXP

Historical data of development triangle of claims by business and branch.					
Year of claim					
Claim provisions and payments	Previous year (Year t-4)	Previous year (Year t-3)	Previous year (Year t-2)	Previous year (Year t-1)	Previous year (Year t)
	2010	2011	2012	2013	2014
In the same year	8,552,782	12,655,880	11,810,101	63,423,145	250,603,459
One year later	11,409,440	18,738,503	67,408,053	318,515,619	-
Two years later	27,814,551	124,523,135	336,716,620	-	-
Three years later	143,964,012	424,782,765	-	-	-
Four years later	423,779,315	-	-	-	-
	-	-	-	-	-
Total claims estimate	615,520,100	580,700,284	415,934,773	381,938,764	250,603,459
Paid claims	374,061,146	379,701,831	256,278,408	267,751,047	147,556,530
Claim provisions	241,458,954	200,998,452	159,656,365	114,187,716	103,046,929
Earned premium	1,647,706,621	1,703,183,069	1,338,586,895	1,395,306,374	1,115,261,945

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

NOMINA SEGURA SB077

MXP

Historical data of development triangle of claims by business and branch.					
Year of claim					
Claim provisions and payments	Previous year (Year t-4)	Previous year (Year t-3)	Previous year (Year t-2)	Previous year (Year t-1)	Previous year (Year t)
	2010	2011	2012	2013	2014
In the same year	-	-	-	665,236	179,642
One year later	80,280	-	258,833	770,403	-
Two years later	-	3,476,782	2,382,015	-	-
Three years later	35	1,008,698	-	-	-
Four years later	744,673	-	-	-	-
	-	-	-	-	-
Total claims estimate	824,988	4,485,480	2,640,848	1,435,639	179,642
Paid claims	102,818	208,730	160,879	117,499	4,950
Claim provisions	722,170	4,276,751	2,479,969	1,318,140	174,692
Earned premium	10,073,971	8,043,722	6,244,766	5,421,424	3,676,418

VIDA GRUPO Y COLECTIVO SB077

MXP

Historical data of development triangle of claims by business and branch.					
Year of claim					
Claim provisions and payments	Previous year (Year t-4)	Previous year (Year t-3)	Previous year (Year t-2)	Previous year (Year t-1)	Previous year (Year t)
	2010	2011	2012	2013	2014
In the same year	2,097,003	8,548,184	12,564,127	56,438,911	154,086,401
One year later	5,325,312	11,616,391	54,980,560	181,539,930	-
Two years later	12,373,487	53,734,268	140,818,125	-	-
Three years later	61,373,768	160,450,616	-	-	-
Four years later	161,680,567	-	-	-	-
	-	-	-	-	-
Total claims estimate	242,850,136	234,349,457	208,362,813	237,978,841	154,086,401
Paid claims	164,316,541	158,849,492	149,240,977	186,451,772	109,451,334
Claim provisions	78,533,595	75,499,966	59,121,836	51,527,070	44,635,067
Earned premium	374,607,261	382,608,634	406,103,346	420,873,867	382,307,501

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

ACCIDENTES PERSONALES SB077

MXP

Historical data of development triangle of claims by business and branch.					
Year of claim					
Claim provisions and payments	Previous year (Year t-4)	Previous year (Year t-3)	Previous year (Year t-2)	Previous year (Year t-1)	Previous year (Year t)
	2010	2011	2012	2013	2014
In the same year	386,057	2,357,948	1,265,000	3,568,582	13,577,169
One year later	770,000	2,122,594	9,928,693	24,776,141	-
Two years later	1,005,639	18,305,902	43,747,040	4,808	-
Three years later	13,655,074	36,425,301	-	-	-
Four years later	28,878,405	-	-	-	-
	-	-	-	-	-
Total claims estimate	44,695,175	59,211,745	54,940,733	28,349,531	13,577,169
Paid claims	29,226,602	29,593,549	29,129,363	20,663,032	7,137,950
Claim provisions	15,468,572	29,618,195	25,811,370	7,686,499	6,439,219
Earned premium	294,535,513	309,813,783	275,122,056	208,629,363	147,216,810

**GTOS MEDICOS
SB077**

MXP

Historical data of development triangle of claims by business and branch.					
Year of claim					
Claim provisions and payments	Previous year (Year t-4)	Previous year (Year t-3)	Previous year (Year t-2)	Previous year (Year t-1)	Previous year (Year t)
	2010	2011	2012	2013	2014
In the same year	13,000	4,500	337,000	5,385,250	33,132,500
One year later	2,000	121,000	1,548,500	8,385,000	-
Two years later	170,421	1,472,750	4,603,500	-	-
Three years later	1,442,997	5,199,000	-	-	-
Four years later	5,509,132	-	-	-	-
	-	-	-	-	-
Total claims estimate	7,137,550	6,797,250	6,489,000	13,770,250	33,132,500
Paid claims	3,861,076	3,452,250	3,451,000	9,531,500	20,130,500
Claim provisions	3,276,474	3,345,000	3,038,000	4,238,750	13,002,000
Earned premium	124,179,479	163,513,810	119,109,467	98,169,040	107,462,185

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

INCENDIO SB077

MXP					
Historical data of development triangle of claims by business and branch.					
Year of claim					
Claim provisions and payments	Previous year (Year t-4)	Previous year (Year t-3)	Previous year (Year t-2)	Previous year (Year t-1)	Previous year (Year t)
	2010	2011	2012	2013	2014
In the same year	-	-	-	-	-
One year later	-	-	584,569	246,696	-
Two years later	234,159	152,450	3,144,260	-	-
Three years later	37,920	4,682,442	-	-	-
Four years later	4,438,273	-	-	-	-
	-	-	-	-	-
Total claims estimate	4,710,352	4,834,892	3,728,829	246,696	-
Paid claims	3,487,935	3,733,569	2,377,303	45,727	-
Claim provisions	1,222,417	1,101,323	1,351,526	200,969	-
Earned premium	39,449,716	38,397,909	40,276,954	11,958,832	-

DIVERSOS SB077

MXP					
Historical data of development triangle of claims by business and branch.					
Year of claim					
Claim provisions and payments	Previous year (Year t-4)	Previous year (Year t-3)	Previous year (Year t-2)	Previous year (Year t-1)	Previous year (Year t)
	2010	2011	2012	2013	2014
In the same year	14,000	2,000	44,000	1,570,935	8,292,000
One year later	14,000	17,000	3,709,495	9,647,317	-
Two years later	31,676	- 26,890	3,097,955	-	-
Three years later	381,127	2,796,491	-	-	-
Four years later	8,898,338	-	-	-	-
	-	-	-	-	-
Total claims estimate	9,339,141	2,788,602	6,851,450	11,218,252	8,292,000
Paid claims	4,950,994	1,648,661	2,048,913	2,047,465	1,670,000
Claim provisions	4,388,147	1,139,940	4,802,537	9,170,787	6,622,000
Earned premium	42,207,538	52,638,702	23,232,477	22,405,493	23,277,671

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

RESPONSABILIDAD
CIVIL SB077

MXP

Historical data of development triangle of claims by business and branch.					
Year of claim					
Claim provisions and payments	Previous year (Year t-4)	Previous year (Year t-3)	Previous year (Year t-2)	Previous year (Year t-1)	Previous year (Year t)
	2010	2011	2012	2013	2014
In the same year	-	-	-	-	-
One year later	-	-	51,421	36,413	-
Two years later	-	50	413,341	-	-
Three years later	403,112	114,891	-	-	-
Four years later	541,081	-	-	-	-
	-	-	-	-	-
Total claims estimate	944,193	114,941	464,762	36,413	-
Paid claims	772,623	67,713	278,777	3,880	-
Claim provisions	171,570	47,228	185,985	32,533	-
Earned premium	70,176,897	61,485,226	18,748,131	5,919,201	-

TERREMOTO
SB077

MXP

Historical data of development triangle of claims by business and branch.					
Year of claim					
Claim provisions and payments	Previous year (Year t-4)	Previous year (Year t-3)	Previous year (Year t-2)	Previous year (Year t-1)	Previous year (Year t)
	2010	2011	2012	2013	2014
In the same year	-	-	-	-	-
One year later	-	-	36,464	57,320	-
Two years later	12,220	178,649	1,344,210	-	-
Three years later	71,168	727,604	-	-	-
Four years later	1,905,164	-	-	-	-
	-	-	-	-	-
Total claims estimate	1,988,552	906,253	1,380,674	57,320	-
Paid claims	619,877	26,591	189,941	-	-
Claim provisions	1,368,675	879,662	1,190,733	57,320	-
Earned premium	69,094,673	67,835,576	62,080,033	18,902,152	-

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

**AUTOMOVILES
SB077**

MXP

Historical data of development triangle of claims by business and branch.					
Year of claim					
Claim provisions and payments	Previous year (Year t-4)	Previous year (Year t-3)	Previous year (Year t-2)	Previous year (Year t-1)	Previous year (Year t)
	2010	2011	2012	2013	2014
In the same year	39,105	831	89,907	514,172	2,240,678
One year later	-	142,586	141,173	4,379,729	-
Two years later	-	65	3,226,816	-	-
Three years later	16,565	633,961	-	-	-
Four years later	209,974	-	-	-	-
	-	-	-	-	-
Total claims estimate	265,644	490,478	2,995,737	4,893,901	2,240,678
Paid claims	187,735	379,601	891,292	10,615,264	1,796,822
Claim provisions	77,909	870,079	3,887,029	5,721,363	443,857
Earned premium	481,415,170	416,385,735	397,447,785	79,678,506	60,450

(32) Commitments and contingent liabilities-

(a) Leases-

Certain premises and equipment are leased. Lease agreements provide for regular adjustments to rent amounts based on changing economic factors. Total lease expense amounted \$1,027 in 2014 and \$1,482 in 2013.

(b) The Group has executed a distribution agreement with Principal Afore, S. A de C. V., Principal Grupo Financiero, in which there is a commitment to distribute on an exclusive basis its products through the Group branches over a five-year period, ending in 2016.

(c) On March 7, 2012, the Bank signed a distribution agreement with AXA Seguros, S. A. de C. V., whereby the Bank agrees to the exclusive distribution of general insurance products in exchange for an agreed-upon commission. The term of the agreement is 10 years from April 2013.

(d) Lawsuits and litigation -

The Group is involved in a number of lawsuits and claims arising in the normal course of business. It is not expected that the final outcome of these matters will have a significant adverse effect on the Bank's financial position and results of operations.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

In accordance with FRS C-9 liabilities, provisions, contingent assets and liabilities and commitments, the Group classifies its legal obligations in:

- Probable: When the possibility of future event occurs is high (probability of loss greater than 50%);
- Possible: The possibility that the future events occurring is more than remote but less than likely (probability of loss greater than 5% and less than 50%);
- Remote: The possibility that the future events occurring is low (probability of loss greater than 5%).

At December 31, 2014 and 2013, the Group presented in the consolidated financial statements the recognition of liabilities for this purpose for an amount of \$433 and \$274 respectively, which correspond to cases in which it was considered that the possibility of loss would likely be probable. The Group at December 31, 2014 and 2013 had outstanding cases with a possible loss contingency in the amount of \$59,250 and \$59,348, respectively.

The Group has contingent liabilities in disputes with third parties, which have not been disclosed pursuant the related financial reporting standards, given that the administrative procedure is at an initial stage and no resolution has been issued yet.

(33) Bank risk management (unaudited)-

Within the Group of HSBC in Mexico the comprehensive risk management involves both compliance with Prudential Provisions on the Subject of Comprehensive Risk Management included in the “Circular Unica” issued by the Banking Commission and the worldwide Group regulations established by HSBC Holding PLC (HGHQ), whose ultimate purpose is generating shareholder value, whilst maintaining a conservative profile in respect of exposing the organization to risk.

The recognition of fundamental concepts is essential for efficient and effective comprehensive management of risks, both quantifiable and discretionary (credit, market and liquidity) and non-discretionary: operational (technology and legal) and under the premise that basic identification, measurement, monitoring, limitation, control and divulging processes are fulfilled.

As in its principal affiliates, the Group's risk management function begins with the Board of Directors, who has primary responsibility for approving the related objectives, guidelines and policies and for determining the risk exposure limits, which is supported by the Assets and Liabilities Committee (ALC) and the Risk Management Committee (RMC).

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

Assets and Liabilities Committee (ALCO)

This Committee meets on a monthly basis and is chaired by the Group's Executive President and General Director. Committee members include senior bank executives from areas such as: Retail, Corporate, Business and Commercial and support areas such as: Treasury, Finance, Risks, Treasury Operations, Balance Sheet Management and Planning. Similar structures are maintained at other affiliates.

The ALC is the prime vehicle for attaining the objectives of an adequate management of assets and liabilities. Its principal purposes concerning risks are as follows:

- Providing strategic management and ensuring tactical follow-up by creating a balance sheet structure that integrates objective compliance within the pre-established risk parameters.
- Identifying, monitoring and controlling all relevant risks, including the information generated by the RMC.
- Distributing the necessary information for proper decision making.
- Conducting overall reviews of sources and destination of funds.
- Determining the most likely environment for the Bank's assets and liabilities in planning and considering contingency scenarios.
- Evaluating alternatives for: rates, prices and portfolio mixes.
- Reviewing and becoming accountable for: distribution and maturity of assets and liabilities, position and size of interest margins, liquidity levels and economic utility.

For reinforcing decision making, the local ALCOs as is the case of Mexico's report directly to the Group's Central Finance Direction of HGHQ.

Risk Management Committee (RMC)

The Risk Committee is responsible to the Board of Directors. The Committee may meet with the frequency with which it is deemed necessary. It is expected that the Committee sessions on a monthly basis, and is usually held the third week of the month.

(Continued)

GRUPO FINANCIERO HSBC, S. A. DE C. V. AND SUBSIDIARIES

Notes to Consolidated Financial Statements

(Millions of pesos)

In response to the regulatory Dispositions and in order to have independent opinions to the Bank's management, the Risk Committee is composed of three external counsellors, and senior managers of the Bank, including the CEO, Deputy CEO of Risk, Deputy CEO of Audit, Deputy CEO of Consumer Banking, Deputy CEO of Commercial Banking, Deputy CEO for Global Banking, Deputy Corporate CEO and CTSO, Deputy CEO of Finance, Head of Legal, Head of Global Markets, Chief Risk in Latin America and Secretary. The Committee is chaired by an external Counsellor.

The major Committee objectives, which are shared with Group affiliates, are as follows:

- Monitoring of current and potential risks that could impact the operation of the Bank, its realization and evaluate the potential impact they might have, either reputational, financial or operationally. You must also develop a focused and integrated approach to identifying them.
- Propose solutions to improve early risk profile and review strategies for risk mitigation.
- Develop a clear profile and trends in credit, market, liquidity, insurance, operational, reputational and internal controls that could impact or cause changes in business strategy.
- Establish a process focused on risk management of relevant risks, contingencies and mitigating and consolidate reporting risks ALCO review.
- Approve and propose to the Board changes in rules and policies on Risk Management, in accordance with the regulation that sets the Banking Commission.
- Authorize the maximum tolerance to market risk, credit risk and other risks considered acceptable in terms of treasury operations (derivatives).
- Review and approve the goals, operations and control procedures, and the level of risk tolerance, based on market conditions.
- Authorize the terms of reference of committees depend on it, including the authorization of its members and provide them with guidance and supervision in their activities.
- Approve the methodologies for measurement and identification of all risks.
- Oversee the approval of new products as well as subsequent revisions and amendments.
- Approve changes in the methodologies for provisions, economical factors and emergency periods.

(Continued)

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- Review important topics that are open, which will be included in the certification of the Director General (depending on time of certification), likewise, should monitor the resolution of these issues.
- Develop and modify the objectives, guidelines and policies origination and credit administration.
- Designate and remove the Chief Officer of the Comprehensive Risk Management Unit. Both designation and removal shall be ratified by the Board of Directors.
- At least on a quarterly basis, communicate to the Board of Directors the risk exposure assumed by the Bank, as well as the failure of the risk exposure limits and risk appetite.
- Ensure all those involved in assuming risks are aware of the exposure limits and the risk tolerance levels.
- Management of Credit Risk, Market Risk, Liquidity, Insurances, Asset Management, Private Banking, Reputation, Sustainability, Strategy, Operational Risk, and Internal Control, including Financial Crime Compliance, Regulatory Compliance and Security & Fraud, as well as Audit matters, which have local, regional or global impact on the Bank.
- Monitor the current risks that might have an impact on the legal entities comprising the Group, at the frequency defined for each entity.

Market Risk

Qualitative information

a) Description of qualitative issues related to the Comprehensive Risk Management process.

The objective of the Group's market risk management function is to identify, measure, monitor, limit, control, inform and disclose the various risks to which the institution is exposed.

The Board of Directors establishes the RMC, whose objective is to manage the risks to which the institution is exposed, and to oversee that transactions adhere to the risk management purposes, policies and procedures and the global and specific risk exposure limits previously approved by the Board of Directors.

Market risk, as defined by the institution, is the "risk that market prices and rates on which the Bank has taken positions – interest rates, foreign exchange rates, stock prices, etc. – move adversely relative to positions taken, thus causing losses to the Group; that is, the potential loss arising from changes in risk factors relating to the valuation or expected results of assets, liabilities or contingent liability transactions, such as interest rates, foreign exchange rates, price indexes, among others.

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The main market risks to which the Group is exposed, can be generally classified in accordance with the exposure of its portfolios to variances of the different risk factors, as follows:

- **Currency or exchange risk.**- This risk arises in open positions of currencies other than the local currency, which lead to exposure to potential losses due to variances in the exchange rates involved.
- **Interest rate risk.**- This risk results from having to maintain assets and liabilities (real, nominal or notional) with various maturity or depreciation dates. Thus, exposure to changes in the interest rate levels is created.
- **Stock risk.**- This risk emerges from maintaining open positions (purchase or sale) with stock or stock-based instruments. Thus, exposure to changes in the market price of stock or stock-based instruments is created.
- **Volatility risk.**- The volatility risk is related to financial instruments with options so that their price depends, among other factors, on volatility perceived in the option's underlying asset (interest rate, stock, exchange rate, etc.).
- **Base or margin risk.**- This risk arises when an instrument is used as hedge of another one and each is valued using different rate curves (for instance, a government bond hedged by an interbank rate derivative) so that the market value may differ leading to hedge imperfections.
- **Credit Risk Margin.** -it is the risk of incurring losses in the price of corporate bonds, bank or sovereign in foreign currency for credit changes in the credit perception of the issuer.

b) Principal elements of market risk management methodologies.

The Group measures elected to identify and quantify the Market Risk exposure are Value at Risk (VaR) and "Present Value of a Basis Point" (PVBP) calculations, which measure the sensitivity to interest rates. Both risk measures are monitored on a daily basis compared to market risk exposure limits duly approved by Management. Additionally, stress testing is performed. Furthermore, it is important to mention that to calculate VaR and PVBP, all of the Bank's positions are marked to market.

Value at Risk (VaR)

The VaR is the statistical measure of a portfolio's maximum potential loss arising from changes in market risk factors of the financial instruments for a given holding period. Therefore, the VaR calculation is based on specific levels of confidence and holding periods. Since January 2006, the VaR is obtained by Historical Simulation with total valuation, considering 500 historic changes in the market risk factors.

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The Board of Directors, at the Risk Committee's proposal, has set a confidence level of 99% with a 1-day holding period; accordingly, the VaR level represents the maximum loss that that the Bank could possible experience in one day with a 99% probability.

Present Value of a Basis Point (PVBP) and Forward PVBP (F-PVBP)

The PVBP is a technique to measure the market risk exposure resulting from changes in interest rates. This measure shows the potential loss that results from a one basis point change in interest rates used to determine the price of financial assets and liabilities, marking to market all of the positions in financial instruments sensitive to interest rates.

The purpose of the Forward PVBP (F-PVBP) is to measure the effect of interest rate changes on financial instruments subject to interest rates. In this sense, the F-PVBP is based on the assumption of a scenario in which the forward rates implied in the curve increase by one basis point.

Surcharge risk

By surcharge risk we understand the potential adverse fluctuation in the value of positions of financial instruments with surcharge (floating government bonds) due to market fluctuations in such risk factor.

Base risk

Base risk is the term used for describing the risk that exists for the movement of a market (due to internal factors) with respect to others. The base risk increases when an instrument is used for hedging another one and the instrument prices are set by two different interest rate curves.

These differences are caused by the various existing characteristics between markets, which are:

- Regulation
- Individual market restrictions
- Calendars
- Conventions (basis in rates)
- Others

Credit Spread (CS01)

The Credit Spread Risk or CS01 is used to control the risk of keeping the bonds issued by the private sector, the value of which may vary due to changes in the credit rating of the issuers.

Such credit rating is reflected in the profit differential with respect to sovereign bonds. HSBC employs market risk limits to control the sensitivity that value may experience in these positions due to changes in the credit rating of issuers.

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Vega or Volatility Risk

The Group takes positions in instruments that are sensitive to changes in implicit market volatility, such as interest rate options and foreign exchange. Vega limits are used to control the risks associated with such market volatilities.

Stress testing

This is a technique that takes into consideration extreme values occurring isolatedly but which are unlikely based on the distribution of probabilities assumed for the market risk factors, but in case it happens this could generate from moderate to severe impacts. The generation of stress testing scenarios for analyzing the sensitivity of the Bank's positions and the interest rate risk exposure is performed on the basis of hypothetical scenarios. Both positive and negative changes are considered to measure the impact on the portfolios.

At the same time, the base PVBP forward is linearly extrapolated to the hypothetical scenarios (assuming that the portfolio is perfectly linear) so as to compare both calculations and obtain the implied convexity. In addition stress tests are performed in relation to exchange rates and share prices.

Methods for Validation and Calibration of Market Risk models

In order to detect in a timely manner any decrease in the prediction quality of the model, automatic data loading systems are in place, thus preventing manual data inputting. Furthermore, for the purpose of measuring the efficiency of the VaR estimation model, back-testing is performed. This type of test allows verification that the maximum estimated losses, on average, do not exceed the reliability level established, comparing the profits/losses that would have been generated had the portfolio been held during the VaR holding period. Back-testing is reinforced by performing hypothesis testing procedures.

As for the PVBP, it has been compared with the sensitivity of the portfolios to market quotations. The results of these tests confirm the accuracy of the models. In order to reinforce the validation and verification of the various risk factors, a set of matrices has been designed that show the behaviour of different risk factors selected in order to check their reasonableness in relation to the values prevailing in the financial markets and verify the current value and the value on the preceding business day for consistency.

Portfolios subject to VaR and PVBP calculation

For a detailed and precise portfolio management, and adhering to the international (IAS) and local (Local GAAP) standards or effective market risk management, the Market Risk management of HSBC Mexico has perfect control of the portfolio structure. Such specific classification should at all times be comprehensible from an accounting viewpoint. This allows for calculating the risk measures (sensitivity, potential loss and stress measures) for any sub-portfolio aligned with the accounting.

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The market risk area calculates the VaR and PVBP for the Bank's total portfolio and specific Accrual and Total Trading portfolios so as to monitor the Bank's own and trading positions.

Global VaR is estimated for each portfolio. Additionally, VaR is broken down by risk factors (Interest Rates and Foreign Exchange Rates and Interest rate, FX and Shares volatilities).

PVBP is presented by segment of the forward curve (Buckets), for both peso and dollar interest rates (Accrual and Trading Intent).

Stress testing is performed for the Bank's portfolio and the "Total Trading" and "Accrual" portfolios, furthermore, a special stress test is performed for Available for Sale (AFS) and Hedging Securities (CSH and FVH).

Quantitative information

As follows it is going to be presented, the Group's VaR and PVBP and the Total Trading and Accrual portfolio sub-division of "Trading Intent" and "Accrual" for the 4Q of 2012 (in million of dollars). The VaR & PVBP limits shown correspond to the latest updating of Market Risk Limits approved by the Group's Board of Directors and the Risk Committee.

Value at Risk (VaR) (All risk factors being considered)

	<u>Bank</u>		<u>Total Trading</u>		<u>Accrual</u>	
	Average		Average		Average	
	Q4		Q4		Q4	
	<u>2014</u>	<u>Limits*</u>	<u>2014</u>	<u>Limits*</u>	<u>2014</u>	<u>Limits*</u>
Total	13.04	38.00	3.69	13.00	11.39	38.00
Rates	11.77	40.00	3.57	9.50	10.84	38.00
Credit margin	3.32	22.00	0.81	3.00	2.42	22.00
Exchange rates	1.04	5.00	1.04	5.00	N/A	N/A
Interest rates volatility	0.09	4.00	0.09	1.80	-	2.50
FX rates volatility	0.07	2.00	0.07	2.00	N/A	N/A
Equities	0.01	2.50	0.01	2.50	N/A	N/A

* Absolute value, N/A = Not applicable

* Global Market Value at Risk (VaR) (Compared to last quarter)

	<u>September</u>	<u>December</u>		<u>Q3</u>	<u>Q4</u>
	<u>30, 2014</u>	<u>31, 2014</u>	<u>Limits *</u>	<u>2014</u>	<u>2014</u>
				<u>average</u>	<u>average</u>
Bank	14.24	12.28	38.00	13.75	13.04
Accrual	12.60	10.32	38.00	12.32	11.39
Total trading	4.87	2.73	13.00	3.38	3.69

* Absolute value

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The Group's VaR at the end of the fourth quarter of 2014 change 13.76% in respect of the Q3 2014. During the period, VaR levels remained below the limits set by management.

The Group's average VaR for the fourth quarter of 2014 change 5.16% in respect of the average VaR for the 3Q 2014.

Comparison of Market risk VaR to Net Capital

Below a comparative VaR average against Net Capital table as of September 30 and December 31, 2014; in millions of dollars:

	September 30, 2014	December 31, 2014
Total VaR *	13.75	13.04
Net Capital **	3,824.70	3,448.24
VaR / Net Capital	0.36%	0.38%

* Quarterly Average VaR of the Bank (absolute value)

** Net Capital of the Group at the end of quarter

Average market VaR represented 0.38% of net capital in fourth quarter of 2014.

Present Value of a Basis Point (PVBP) for Peso Interest Rate

	Sep 30, 14	Dec 31, 14	Limits *	Average Q3 2014	Average Q4 2014
Bank	(1.076)	(1.171)	2.050	(1.194)	(1.160)
Accrual	(0.902)	(1.144)	1.550	(1.058)	(1.073)
Trading intent	(0.174)	(0.027)	0.500	(0.136)	(0.086)

* Absolute value N/A - Not Applicable

The Group's PVBP in peso rates for the close of the fourth quarter of 2014 varied (8.83%) with respect to the PVBP for the close of the previous quarter. The Group's average PVBP corresponding to the fourth quarter of 2014 varied (2.85%) with respect to the PVBP for the close of the previous quarter.

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Present Value of a Basis Point (PVBP) for Dollar Interest Rates

	<u>Sep 30, 2014</u>	<u>Dec 31, 2014</u>	<u>Limits *</u>	Q3 average 2014	Q4 average 2014
Bank	0.091	0.040	0.430	0.045	0.028
Accrual	(0.014)	0.003	0.300	0.020	0.003
Trading intent	0.105	0.037	0.180	0.024	0.026

* Absolute value N/A - Not applicable

The Group's PVBP in US dollars interest rate at the end of Q4 2014 changed by (56.04%) as compared to the PVBP at the end of Q3 2014. The Group's average PVBP for Q4 2014 changed by (37.78%) as compared to the average PVBP for Q3 2014.

Present Value of a Basis Point (PVBP) for UDIS interest rates

	<u>Sep 30, 2014</u>	<u>Dec 31, 2014</u>	<u>Limits *</u>	Q3 average 2014	Q4 average 2014
Bank	(0.020)	(0.038)	0.150	(0.049)	(0.026)
Accrual	(0.019)	(0.015)	0.050	(0.022)	(0.018)
Trading intent	(0.001)	(0.023)	0.100	(0.027)	(0.008)

* Absolute value

The Group's PVBP in UDIS interest rate at the end of Q4 2014 changed by 90% as compared to the PVBP at the end of Q3 2014. The Group's average PVBP for Q4 2014 changed by (46.94%) as compared to the average PVBP for Q3 2014.

Liquidity risk-**Qualitative information**

Liquidity risk arises primarily from gaps between the maturities of the Institution's assets and liabilities. Customer demand and time deposits mature on dates which differ from those of loans placed and investment securities.

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The Group has implemented liquidity ratio limits both in pesos and dollars. These liquidity ratios are calculated daily and compared to the limits authorized by the Assets and Liabilities Committee and confirmed by the HSBC Group. In addition, the Institution performs a daily review of cash commitments and evaluates the requirements of the principal customers for diversifying the sources of funding.

In addition, Group has implemented a methodology for measuring liquidity risk based on different period cash flow projections and the formulation of liquidity scenarios.

Since 2003, Group implemented a liquidity contingency plan, which defines the potential liquidity-related contingencies and establishes plan responsible individuals, action plan and alternative sources of funding available to the Institution should a contingency arise. During the year, the Assets and Liabilities Committee ratified the plan.

Every year, the Financing Contingency Plan is submitted to the Assets and Liabilities Committee and the Board of Directors for approval. This plan contains all the elements required by the Provisions in Appendix 12C and as required by the Group as a result of international experience; for instance: key factors, crisis management team, specific responsibilities of each team member, potential action plans, alternative sources of payment taking into account availability, capability and costs thereof, internal and external communication plan and forms for notification to the Banking Commission, if activated.

For all the members to be aware of their roles in the Plan, reviews are personally conducted with each one of them on a semi-annual basis, and prior to submission to the Board of Directors for approval.

According to the last amendments published on December 31, 2014 in the Official Gazette, with regard to the Provisions about liquidity requirements for commercial banking institutions, the implementation of a Liquidity Hedge Coefficient is provided in accordance with the proposal made by the Basel Committee. These regulations will become effective from January 1, 2015. In this respect, the Group considers it is prepared for implementing the calculation methodology of such coefficient from the effective date.

Quantitative information

At the end of Q4 2013, the Group liquidity ratios were USD\$1,563 million in term up to 7 days, USD\$2,327 million in a term of a month, USD\$590 million in a term of 3 months; every scenario resulted in a positive cumulated cash flow. This is a reflection of the Entity's adequate cash flow position for the subsequent twelve months.

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During the quarter, average levels were USD\$788 million in 7 days, USD\$1,613 million for 1 month, of USD\$511 million for 3 months. With respect to last quarter's liquidity position was affected by transactions changes made, money market operations and long-term investment.

Credit risk-**Qualitative information**

For managing the credit risk at Group, in addition to following up on the behaviour of the loan portfolio on a regular basis, risk assessment tools are developed, implemented and monitored. The primary objective of managing the credit risk is knowing the quality of the portfolio and taking timely action for reducing potential losses associated with credit risks, complying at the same time with the Group's and Basel II policies and standards as well as Banking Commission's regulations.

Credit risk is defined as the risk of financial loss if a customer or counterparty fails to meet an obligation under a contract with a Group member or members, that is, the potential loss on lack of payment by a borrower or counterparty. For the proper measurement of the credit risk HSBC has credit risk quantification methodologies as well as advanced information systems.

In general, the methodologies separate client risk (probability that a client defaults its payment obligations: Probability of Default) from credit or transaction risks (risk inherent to the structuring of the loan, which mainly includes the value and type of security).

In addition, the Group has developed policies and procedures that comprise the various loan process stages: assessment, authorization, granting, control, follow-up and recovery.

- a) Model and systems used for the quantification and management of credits risk:

Commercial portfolio**1. Allowance for loan losses**

Since June 2013, the Group adopted the new rules for estimating preventive reserves established by the CNBV in the Provisions, except for the preventive creation for credit risks corresponding to credits granted to financial entities, which were adopted in March 2014, which set forth an expected loss methodology.

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Administrative models

The Group has various models for internal risk management, developed to encompass the three key parameters of credit risk:

1. Probability of default
2. Loss given default
3. Exposure at default

These models are evaluated and monitored on a quarterly basis to assess their performance and their proper application, so that the follow-ups are carried out in a timely manner.

Regarding the models of Probability of Default (PD), monitoring is aimed at testing the differentiation between customers that comply with their obligations to the Group and those which do not, and will order them by the appropriate risk levels. Moreover, it validates the quantification model and compared with observed default rates to meet its accuracy.

On the other hand, for models of Exposure at Default and Loss Severity, it is validated the estimates on the loss that may be incurred by the institution in case that the client fail, are accurate with sufficient conservatism.

It is important to note that each version of the models is reviewed and approved according to standards set by the Group.

a) Probability of default model (PD)

During 2014, HSBC México developed a new model for risk rating of business and corporate clients with annual sales for more than \$40 and less than \$12,500, which was implemented on January 8, 2015. This model derived from the statistical analysis of different explanatory factors of default probability: economic, financial and qualitative, differing from those confirmed by size.

It is important to note that these models were reviewed and approved by experts in model developing of HGHQ.

In addition to the above models, the Group has implemented the following global models that were developed by HGHQ.

- A model to evaluate the global clients (GLCS), applicable to mayor corporate offices with sales equal to or greater than USD \$12,500.
- A model for banking financial entities (RAfBanks).
- Eleven models for non-banking financial entities (NBFI Models DST).

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The implementation of the models mentioned in the previous paragraphs was accompanied by a new level of customer risk rating known as Customer Risk Rating (CRR), which consists of 23 levels, of which two are for customers in default.

This scale has a direct correspondence to Probabilities of Default and allows sufficient granular measurement of the creditworthiness of customers.

The default probability models included in the internal rating system are monitored quarterly with the aim of checking its proper performance, and if the results of this monitoring are not the expected according to Bank standards action plans are established to meet the established guidelines.

In the results of the last monitoring for commercial portfolio models developed locally (for corporate head offices with annual sales of up to \$12,500), an inappropriate performance of the model is noticed. As mitigating actions, a new model of Default Probability has been developed under the HGHQ Global Standards, which is expected to be implemented beginning 2015.

The rest of the global models, GLCS, RAf Banks and NBFi DST are low default models so it is currently not possible to measure their performance; however, override rates are being monitored, which are within the tolerances set out by the HGHQ.

b) Model of estimation of Loss Given Default (LGD)

Regarding the estimation of Loss Given Default (LGD), which represents the economic loss as a percentage of exposure to default that will face the Bank at the time that a customer defaults, the Bank developed a local model for business and corporate clients. Similarly, for banking financial institutions, the Bank has implemented a model developed by HGHQ.

The most recent monitoring of the LGD local model shows a relatively low correlation (20.21%) between the observed and the estimated Severity; therefore, the model is currently in the process of being redeveloped and it is expected to conclude it during 2015.

c) Model of exposure at default (EAD)

For estimating the Exposure at Default (EAD), the Group also developed a model for local business and corporate customers. It is also estimated the exposure at default of banking financial institutions based on the guidelines established by the Group.

The most recent quarterly performance monitoring for this model showed a relatively low correlation (22.90%) between the values of the observed and the estimated EAD. Thus, the model is currently in process of redevelopment and it is estimated to be completed by 2015.

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2. Risk assessment system

In order to establish a better infrastructure, management and measurement of credit risk for commercial loans, the Bank uses the assessment tool Moody's Risk Analyst (RA), which allows an assessment of the credit quality of the customers based on their financial and qualitative information.

Furthermore, HSBC has a system worldwide for managing, controlling and better following up on the commercial loan approval process in Commercial Banking known as *Credit Application and Risk Management* (CARM), used for approving most loan applications. This system allows for finding out the status of the loan application during and process stage.

Additionally, and in order to improve the administration of the guarantees of commercial loans, since 2006 the Bank has been using the system called Fair II. Finally, it is important to note that it also has a system that controls and limits the use of credit lines from approval Lines III.

In order to ensure consistency in the local provisioning process of the Commercial Portfolio, including Financial Entities, the Credit Reserves application was implemented in the Bank during the first quarter of 2014.

Quantitative information

The expected loss of the portfolio of commercial loans at December 31, 2014 is \$12,747, showing an increase of \$330 (3%) over the previous quarter. The average balance of commercial loans at December 31, 2014 is \$192,752 with an increase of \$13,848 (7.74%) compared to that reported in the previous quarter.

Below are average balances and the expected loss of the commercial portfolio by business line:

Line of business	Average balances for the 3 month period		VAR		Balances		VAR		Expected loss		VAR	
	Q32014	Q42014	(\$)	(%)	Sep-14	Dec-14	(\$)	(%)	Sep-14	Dec-14	(\$)	(%)
CMB	\$96,030	\$99,309	\$3,279	3%	\$95,666	\$100,314	\$4,648	5%	\$10,366	\$10,579	\$213	2%
GBM	\$82,089	\$92,760	\$10,672	13%	\$82,929	\$100,770	\$17,841	22%	\$2,051	\$2,168	\$117	6%
GBP	\$786	\$683	(\$103)	(13%)	\$783	\$623	(\$160)	(20%)	\$0.067	\$0.046	(\$0.02)	(31%)
Total	\$178,905	\$192,752	\$13,848	7.74%	\$179,378	\$201,707	\$22,329	12%	\$12,417	\$12,747	\$330	3%

Balance and average balance include contingent exposures.

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Portfolio of consumer credit and mortgage:

Qualitative information

An efficiency assessment of consumer and mortgage loan originating models is performed on a quarterly basis, for verifying that the population being assessed by the model is similar to the population used for constructing the model, that the model continues to have the ability to distinguish delinquent customers from those who are not and that the model continues to award high ratings to customers with lesser risk. The model is recalibrated or replaced when an efficiency deviation is detected.

As part of the management of the consumer and mortgage loan portfolios monthly reports are issued for measuring creditworthiness. Reports are segmented by product and include general portfolio statistics, measures of distribution by level of default, default measures by date of opening, transition reports by level of default, etc. Also, the portfolio expected loss is determined monthly. The expected loss model currently being used considers a two-dimensional approach where each loan is assigned a Likelihood of Default and a percentage of Severity of Loss. The model is calibrated for estimating losses expected over an annual horizon and was prepared using the previous portfolio experience.

Quantitative information

The expected loss for the commercial portfolio of consumer credit and mortgage at December 31, 2014 is \$4,517.

Operational risk-

Qualitative information

Operational risk is the risk of loss arising from internal processes, people and systems failure or external events including technological and legal risks.

The corporate governance structure which underpins the function is complemented by the Risk Management Committee ("RMC") is responsible for compliance with the relevant applicable standards and regulations as well as knowing and understanding the risk profile of the Bank, establishing the risk management priorities, evaluating the strategies and plans for risk mitigation and to monitor risk exposure and mitigation measures on an ongoing basis.

The scheme HGHQ operational controls is based on "three lines of defence", in order to ensure that risks and controls are properly managed global business areas, support areas and the area of global technology services (HTS) continuously. The model establishes administrative responsibilities based on risk management and control environment. The model of the three lines of defence should be applied with common sense, considering the business structures and HGHQ support.

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First line of defence

The first line of defence comprises predominantly managing global business areas and HTS, which are responsible for their activities, processes and controls should be checked daily. It also includes the supporting areas though not in business advisory activities but in specific responsibilities.

This first line includes all the employees' responsibility for being aware of the operational risks and operational risk incidents during the execution of daily activities. Likewise, the Business Unit Directors/supporting areas are responsible for managing operational risk by the processes surrounding them. Management of operational risk primarily includes:

- Identify and evaluate operational risks and controls in accordance with the Risk and Control Assessment policy.
- Identify and present incident reports in accordance with the respective internal policy, and establish mitigating actions to avoid future reiteration.
- Identify control issues inherent to activities and set up action plans to resolve them, or formalize risk acceptance processes when it is not viable to implement such plans.

Line managers shall also identify and evaluate operational risks and controls as part of the decision-making process. Key operational risks and controls shall be continuously monitored, including the following:

- Critical process risks and controls
- Main project risks and controls
- Business acquisition and due diligence implementation
- Business initiatives, including new products or significant changes to existing products
- Planning and budget processes
- Subcontract agreements, supplier selection and internal product utilization.

In order to monitor the foregoing, officers may be designated to monitor control compliance, "Business Risk Control Management (BRCM)", for key businesses and processes within the first line to supervise the implementation of the operational risk management framework.

The monitoring of key controls may be attained through different methods, which include a thematic review of specific processes, the testing of specific controls in several processes or following up of Key Risk Indicators (KRI).

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The BRCMs must develop a monitoring plan of suitable depth each year, which must establish the monitoring activities to be carried out the following year. The plan should be subject to continuous review and updating as circumstances change, in order to ensure that monitoring is in agreement with the Financial Group's risk profile.

Second line of defence

The second line of defence comprises mainly global support areas whose function is to verify compliance with the statement of risk appetite HGHQ. Your responsibilities are:

- Ensure, monitor and exceed the effectiveness of risk and control activities carried out by the first line;
- Develop frameworks to identify and measure the risks assumed by the parties respective business area;
- Monitor the performance of key risks through key indicators and monitoring programs / safety in relation to risk appetite and tolerance levels defined.

Furthermore, global support areas must maintain and monitor controls which are directly responsible.

Third the line defence

The third line of defence is to provide independent assurance by Internal Audit regarding the effectiveness of the design, implementation and integration of risk management frameworks and management of risks and controls by the first line and monitoring control by the second line.

Quantitative information (including Technology Risk and Legal Risk)

The assessment of operational risks resulting from the evaluation exercise carried out during the period 2013, with the changes and updates made during the 4th quarter of 2014 shows a total of 1,549 relevant risks identified and evaluated, distributed as follows: 7.36% (114) of type "Very high risk", 15.43% (239) of the type "High Risk", 29.50% (457) of the type "Medium risk" and 47.71% (739) of type "Low Risk".

Furthermore, the Financial Group maintains a historical base with Operational Risk data since 2007, where operational loss incidences are recorded.

The appetite for operational risk statement for the Bank is US\$60.81 million for operational losses and is monitored monthly through the BSC, which is presented to the Risk Management Committee.

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Technology risk-

The area of information technology (IT) maintains an adequate control technology risk through the guidelines of the Group related to methodologies and standards: FIMs (Functional Instruction Manual), RBPM (risk-based project management), and BIM (procedures general and local work instructions HTS).

In conjunction with the operation structure, the HTS is also in line with the guidelines of other manuals and procedures, HGHQ; the foregoing is due to the fact that it is the service and technology solution provider entity for the different channels and business lines of the Group.

As part of its governance structure, the Group follows up the topics and requirements of the local authority through its compliance area, where one of its main functions is the constant assessment of the risk and the monitoring of the compliance with local law.

The principal methodologies used in the technological risk valuation are:

- I. Through a streamlined governance structure, safe and reliable: designed to maintain proper control of technological risks and response capabilities for all banking services provided at the various distribution channels. The risk is managed in the high-level committees: HTS Steering Committee, Risk Management Committee (RMC), Operational Risk Management Group (ORMG) and HTS Risk Management Meeting (HTS RMM).
- II. The above is carried out with the updating and testing of different scenarios for the Business Continuity Plans (BCP) and its corresponding disaster recovery plan (DRP) for events that required the positioning of its operation in alternative sites.
- III. Risk and Control Assessment (RCA).
- IV. Information technology project management through the standard tool of the group (Risk-Based Project Management - RBPM), particularly in the software development domain, which is SDLC (Software Development Life Cycle).
- V. Risk management with active participation of the specialized Business Risk and Control Management area (BRCM's), including operation risk management, Sarbanes Oxley (SOX), incidents, internal, external and regulatory audits coordination.
- VI. This is carried out with a measurement tool and control scorecard that enables the measurements of the main objectives defined in its strategic planning, which in general refers to the system availability, the project and budget compliance in terms of time and quality and that are presented in different forums and committees for decision-making purposes.

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Legal risk-

Legal risks which could give rise to financial loss, sanctions or reputational damage, have been defined as follows:

- **Contractual:** This is the risk that the rights or obligations in a contractual relationship are inadequate, including: misrepresentations, documentation, unintended consequences, unintended breaches and enforceability.
- **Litigation:** It consists of the risks to which the Group is subject to when an actual or potential litigation situation occurs, and includes both the exposure and the litigation handling;
- **Legislative:** It is the risk of noncompliance with the laws of the different jurisdictions and includes: the compliance with such regulation and its amendments;
- **Non contractual rights:** It is the risk that assets are not duly appropriated, that other parties breach the rights related to such assets or that the rights of the other party are breached, including infringement of third party rights, ownership interest and legal liability.

On the other hand, policies, controls and procedures are designed to enable the identification, measurement and control of the legal risk in order to avoid potential financial losses and operation errors. The specific risks that are intended to be mitigated are as follows:

- **Contractual Risk Control;** They have procedures to ensure that any document that creates a contractual relationship can be signed on behalf of the institution, unless it is received legal advice internal and / or external, either in relation to the form of the documentation or specifically on the transaction and in most cases, are standardized contracts.

All contracts entered into by any member of the institution that contains restrictions that affect the business must have the authorization of the legal representative with appropriate authority levels. Additionally, there are procedures for the regular review of standard contracts to ensure that they remain properly in the light of any legal change.

- **Litigation: Litigation Risk Control:** Procedures are established to ensure appropriate action in response to the claims against, defend efficiently and effectively, be able to take action with the ability to protect and preserve the rights of the institution and inform the responsible Legal issues on trial.

Practices or procedures are properly documented and in place to ensure that liability is not admitted involuntarily in situations of dispute, and it can not be inferred from any internal correspondence or third parties.

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They have procedures and regulations for the Legal area is immediately reported if there is threat of litigation or whether to proceed against the institution, managing demand subsequent actions.

- **Legislative Risk Control:** There are documented procedures and practices implemented to monitor any new law or regulation proposal and any court case resulting in the need to change existing procedures or documentation in their respective jurisdiction and any other jurisdiction which they are responsible. From this, and with the area of Compliance (Compliance), implemented the necessary changes so that operations continue to be made in accordance with current legislation.
- **Risk Management for Failure no contractual rights:** There are procedures in place to ensure that the legal care at all times the correct use of the Group's brands, local brands, advertisements and copyright.

For a third party to make use of the Group's brands or local brands must be previously validated and approved by the Legal Department.

There is a procedure to verify the legal area when required use of trademarks or proprietary third party advertisements, is duly authorized by the holder.

The legal department takes care at all times that all the artistic or literary works that are generated either by his charge to employees or outside vendors or by subsequent acquisition of proprietary rights, are properly documented.

Also been met institutional policies, procedures have been established about Operational Risk and Internal Control, there have been statutory audit has been carried out the estimation of potential losses arising from adverse judgments and established a base historical data on judicial decisions, its causes and costs.

U.S. regulatory and law enforcement investigations:

In October 2010, HSBC Bank USA subscribed a cease and desist order with the Office of the Comptroller of Currency ("OCC"); and the indirect holding of such company, HSBC North America Holdings ("HNAH") subscribed a cease and desist order issued by the U.S. Federal Reserve Board (the "Orders"). Such orders provide for improvements to establish an effective compliance program in handling risk in the activities of HSBC in the U.S.A., including several topics relating to the U.S. Banking Secrecy Act ("BSA") and compliance of money laundering prevention ("MLP"). Action continues to comply with the Order requirements to ensure their compliance and to maintain effective policies and procedures.

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In addition to the foregoing, in December 2012, HSBC Holdings, HNAH and HSBC Bank USA subscribed agreements with government agencies of the U.S. and U.K. as to deficiencies in the past in complying with LSB, PLD and sanctions acts. Among these agreements, HSBC Holdings and HSBC Bank USA subscribed a 5-year deferred prosecution agreement with the US Department of Justice (“DJ”), with the U.S. Attorney’s Office for the Eastern District of New York and with the U.S. Attorney’s Office for the Northern District of West Virginia (“DPA of USA”), HSBC Holdings subscribed a two-year deferred prosecution agreement with the New York County District Attorney (“FDCNY”) (“DPA of FDCN”) and HSBC Holdings subscribed a cease and desist order; HSBC Holdings and HNAH subscribed the consent of a monetary sanction of the Federal Reserve Board (“FRB”). In addition to the foregoing, HSBC Bank USA subscribed the consent of a monetary sanction of the Department of Treasury’s Financial Crimes Enforcement Network (“FinCEN”) and a diverse monetary sanction of OCC. HSBC Holdings also subscribed an agreement with the Office of Foreign Assets Control (“OFAC”) in regard the historical transactions that involve parties subject to OFAC sanctions and an Undertaking with the UK Financial Services Authority (currently the Financial Conduct Authority Direction (“FCA”) for complying with certain obligations in relation to the PLD in the future and with obligations relating to sanctions.

In accordance with these agreements, HSBC Holdings and HSBC Bank USA made payments for a total of US\$1,921m to the US authorities and continue complying with the outstanding obligations. On July 1, 2013, the United States District Court for the Eastern District of New York approved the DPA of USA and retained jurisdiction for supervising its implementation. In conformity with these agreements with the DJ, the FCA and the FRB, a independent corporate compliance monitor has been appointed (which, for FCA purposes is an “expert” according to section 166 of the US Financial Services and Markets Act), who shall continually assess and examine the effectiveness of PLD compliance and HSBC sanctions as well as progress in implementing obligations in accordance with the relevant agreements. The monitor’s activities, which started on July 22, 2013, are being conducted as planned and are consistent with the terms and requirements set out in the relevant agreements.

Where HSBC Holdings and HSBC Bank USA meet the requirements imposed by the DPA of USA, the charges imposed by the DJ against these entities shall be dismissed after the five-year term relating to the agreement has expired. In like manner, if HSBC Holdings meets the requirements imposed by the DPA of the FDCN, the charges imposed by FDCNY against it shall be dismissed after the two-year term relating to this agreement has expired. Both DJ and FDCNY may initiate actions against HSBC Holdings or HSBC Bank USA in cases where any of these entities violates the terms and conditions of their respective agreements

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HSBC Bank USA also subscribed a separate consent order with the OCC, whereby the former is required to correct the circumstances and conditions observed by the OCC in its last supervision report; furthermore, certain restrictions are imposed on HSBC Bank USA with regard to any acquisition of direct or indirect control of, or investment in any new financial subsidiary or for initiating a new activity in its existing financial subsidiaries, unless it receives prior authorization from the OCC. HSBC Bank USA also subscribed a separate consent order with the OCC that compels it to adopt a global institutional compliance program.

The agreements with US and UK authorities do not exclude the possibility of litigation with regard, among other things, to HSBC's compliance with PLD and LSB laws and sanctions or other regulatory or law enforcement actions relating to PLD, LSB or sanctions not foreseen by the agreements.

(34) Credit policies (unaudited)-

Management constantly reviews the consistency between the objectives, guidelines and policies, supporting infrastructure (processes, appropriate personnel and computer systems) and functions of credit origination and management within the Bank, ensuring at all times, irrespective in carrying out their activities to avoid conflicts of interest, in addition those activities performed by the Comprehensive Risk Management process.

Credit promoting-

Promotion of retail credit (individuals) and commercial (individuals with small business and companies) is performed through a branch, internet and / or other means, according to business areas.

Credit evaluation-

Qualitative and quantitative evaluations to approve and grant the different types of financing is done through individual or parametric methods, using models or opinion of highly qualified personnel that meet the standards of the Basel II and the Banking Commission established independently by the area of credit risk.

Credit approval-

Only the highest level by the Board of Directors are empowered to approve individual commercial loans, who in such case, may be delegated to other local officials experienced, considering the level of risk of potential borrowers and their operations, the afore mentioned in accordance with the procedures established by the Group.

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Credit approval by parametric methods, is performed using automated systems to analyze customer information, based on minimum required information which is standardized data and information, which shed weight for a favourable outcome has been previously defined by the risk area.

Instrumentation-

The legal department is responsible for the implementation of all credit transactions, including processing of all credit contracts, promissory notes and the issuance of the opinion of the legal capacity of their applicants.

Restructuring-

Restructuring may only be made viable projects, avoiding incurred in renewing the operation not to affect the Guarantees. Policy not current Securities shall be released and in case of the possibility of replacing them, they should be the same or better.

As an exception to this policy can restructure clients not showing viability of payment, when by this means improve the Group's position (with partial payments, higher guarantees, correcting problems documentaries).

A restructuring operation is one which is derived from any of the following situations:

- a) Extension of Credit Guarantees of the concerned, or;
- b) Changes to the original terms of the loan or payment schedule, among which are:
 - Changing the stated interest rate for the remaining term of the loan;
 - Currency exchange or unit of account, or
 - Provision of a waiting period for compliance with the obligations to pay under the original terms of the loan, unless the award is granted after the deadline originally agreed, in which case it will be a renewal.

Restructuring is not permitted to hide credit problems or deferral losses.

Renewal

Transactions may be renewed only when the loan term is extended during or at the maturity date, or are settled at any moment with the product coming from another loan contracted with the same entity, in which the same debtor or another person are a party as its patrimonial connection constitute common risks. A loan is not considered renewed when the dispositions are made over the term of a pre-established credit line.

According to the internal policy, the original amount of the loan can be increased when renewed.

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Monitoring, control and recovery-

The rating of the loan portfolio is made according to the methodology and procedures to comply with the Group standards and the Banking Commission.

Credit records are concentrated in specialized facilities and are administered by accredited, while parametric loans are integrated by credit.

Monitoring, administrative or judicial recovery, including the assignment of loan portfolio, involves fair treatment of customers and considering best practices, according to criteria established by the business areas, collections, legal and/or credit risk, as appropriate, as well as the areas and people who perform the role of comprehensive risk management.

To ensure a risk-based approach, that is consistent with the problematic exposure and minimizes potential losses, management requirements and criteria that must be met are established, which responsibility is of the areas of Credit Recovery and Risks.

Officials of the segments are responsible for detecting early warnings of broken profiles of their credit portfolios, as well as gather the necessary information for analysis and monitoring, within the management process.

The control and monitoring of credit activity is complemented by the internal audit function and credit review independent of the business and administrative areas.

(35) Recently issued accounting standards-

On May 19, 2014, the Banking Commission published in the Official Gazette amendments to appendix 33 of the Provisions. Amendments to the accounting standards were intended to achieve consistency between the accounting standards applicable to credit institutions and the international accounting standards.

The most important amendments include:

- Addition or modification of concepts to make them consistent with the local and international standards, which does not imply any changes to the current accounting standards.

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- Modification in the presentation of overdrafts in check accounts of clients who do not have a credit line for such purposes, classifying them as “Other accounts receivable” starting from the effectiveness of the new provisions. They are currently recognized as part of the loan portfolio. Additionally, such overdrafts are considered overdue debts and an allowance for doubtful trade receivables shall be mandatorily created in the total amount of the overdraft at the time of recognition.
- Further detail is required in the disclosure of loan portfolio in the financial statements and related regulatory reports.

The original effective date established by the Banking Commission was July 2014; however, such date has extended many times. As of this date, June 2015 is the new effective date.

The Consejo Mexicano de Normas de Información Financiera, A. C. (CINIF) has issued the FRS and Improvements listed below:

FRS C-3 “Accounts Receivable”- FRS C-3 is effective for years beginning January 1, 2018, and is applicable retrospectively; however, early adoption is allowed on January 1, 2016 provided that it takes place concurrently with the adoption of FRS C-20 “Financing Instruments Receivable”. Some of the primary changes resulting from the adoption of this FRS are as follows:

- Provides that accounts receivable based on a contract are deemed financial instruments. On the other hand, some other accounts receivable, resulting from legal or tax provisions, may include certain characteristics of a financial instrument, such as bearing interest, though these are not deemed financial instruments.
- Sets out that the allowance for doubtful trade receivables shall be recognized as revenue is earned. Thus, the allowance shall be recorded as expenses in the statement of comprehensive income.
- Provides that, from initial recognition, the time value of money shall be considered. Therefore, should the effect of the present value of the account receivable be significant in light of its term, an adjustment must be made to take into consideration such present value.
- A reconciliation between the initial and final balances of the allowance for doubtful accounts is required for each period presented.

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FRS C-9 “Provisions, Contingencies and Commitments”- FRS C-9 is effective for years beginning on or after January 1, 2018; early adoption is allowed on January 1, 2016 provided that it takes place concurrently with the initial adoption of FRS C-19 “Financial instruments payable”. FRS C-9 supersedes Bulletin C-9 “Liabilities, Provisions, Contingent Assets and Liabilities and Commitments”. The first-time adoption of this FRS does not produce accounting changes in the financial statements. Some of the main points covered by this FRS include the following:

- Its scope is reduced by moving the subject concerning the accounting treatment of financial liabilities to FRS C-19 “Financial instruments payable”.
- The definition of “liability” is changed by eliminating the qualifier “virtually unavoidable” and including the word “probable”.
- The terminology employed throughout the standard is updated to standardize its presentation to the rest of the FRS.

FRS C-19 “Financial instruments payable”- FRS C-19 is effective for years beginning on or after January 1, 2018 with retrospective effects and early adoption is allowed on January 1, 2016 provided that it takes place concurrently with the adoption of FRS C-9 “Provisions, contingencies and commitments”, FRS C-3 “Accounts receivable” and FRS C-20 “Financing instruments receivable”- Some of the main points covered by this FRS include the following:

- It provides for the possibility of measuring, subsequent to their initial recognition, certain financial liabilities at fair value when certain conditions are fulfilled.
- Long-term liabilities are initially recognized at present value.
- In restructuring a liability, without the future cash flows for its settlement being substantially modified, the costs and commissions expensed in this process shall affect the amount of the liability and be amortized on a modified effective interest rate basis instead of directly affecting the net income or loss.
- It includes the provisions of IFRIC 19 “Extinguishing Financial Liabilities with Equity Instruments”, which was not provided for by the existing standard.
- The effect of extinguishing a financial liability should be presented as a financial result in the comprehensive statement of income.
- It introduces the concepts of amortized cost in valuing financial liabilities and of the effective interest method based on the effective interest rate.

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FRS C-20 “*Financing instruments receivable*”- FRS C-20 shall be effective for years beginning January 1, 2018, and is applicable retrospectively. Early adoption is allowed on January 1, 2016 provided that it takes place concurrently with the initial adoption of FRS C-3 “Accounts receivable” and supersedes the provisions set forth in Bulletin C-3 in this regard. Some of the main aspects resulting from the adoption of this FRS are as follows:

- Classification of financial instruments within assets. To determine such classification, the concept of intention to acquire and hold financial instruments has been removed. Instead, the concept of business management model is adopted, either for obtaining a contractual yield, generating a contractual yield and selling in order to achieve certain strategic objectives, or generating earnings from the purchase and sale thereof, in order to classify them in accordance with the respective model.
- The valuation effect of investments in financial instruments is also focused on the business model.
- The reclassification of financial instruments is not permitted among receivables, strategic investments, and negotiable instruments, unless the entity changes its business model.
- An embedded derivative that modifies the cash flows of principal and interest is not separated from its host receivable financial instrument. The entire receivable financial instrument shall be measured at fair value, as if it were a negotiable financial instrument.

FRS D-3 “*Employee benefits*”- FRS D-3 is effective for years beginning on or after January 1, 2016 with retrospective effects and early adoption is allowed on January 1, 2015. FRS D-3 supersedes the provisions in FRS D-3. Main changes include the following:

- Direct benefits – The classification of direct short-term benefits was modified and the recognition of deferred Employee Statutory Profit Sharing (ESPS) was ratified.
- Termination benefits – The bases were modified for identifying when payments for the termination of a work relationship actually meet post-employment benefits or when they are termination benefits.
- Post-employment benefits – Among others, the following were modified: the accounting recognition of multi-employer plans; government plans and plans of entities under common control; the recognition of the net defined benefit liability (asset); the bases for determining the actuarial hypothesis in the discount rate; the recognition of the Service Cost of Past Periods (SCPP) and of the Early Settlement of Obligations (ESO).

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- Remeasurements – In recognizing post-employment benefits, the corridor approach is eliminated in the treatment of the plan’s profits and losses (PPL); therefore, they are recognized as accrued and recognized directly in Other Comprehensive Income (“ORI”), requiring their recycling to the period’s net profit or loss under certain conditions.
- Plan Asset Ceiling (PA) – Identifies a plan asset ceiling and specifies which entity contributed funds do not qualify as such.
- Recognition in profit or loss of PM, SR and gains or losses from Early Settlement of Obligations (ESO) – In post-employment benefits, the totality of the Service Cost of Past Periods (SCPP) of Plan Modifications (PM), Staff Reductions (SR) and the gains or losses from Early Settlement of Obligations (ESO) are immediately recognized in profit or loss.
- Discount rate – Establishes that the discount rate of Defined Benefit Obligations (DBO) is based on investment grade corporate bond rates (deep market) and, in their absence, on government bond rates.
- Termination benefits – Requires an analysis as to whether separation payments qualify as termination benefits or are actually post-employment benefits and notes that if the benefit is non-cumulative with no preexisting granting conditions, it is a termination benefit and, therefore, it should be recognized when the event occurs. However, if preexisting conditions are present, either contractually, by law or payment practices, it is deemed a cumulative benefit and should be recognized as a post-employment benefit.

2015 FRS Improvements

In December 2014, CINIF issued the document referred to as “2015 FRS Improvements”, which contains precise modifications to some FRS. The modifications that bring about accounting changes are listed below:

FRS B-8 “Consolidated or combined financial statements”- FRS B-8 defines investment entities and stipulates that, in view of the characteristics of such entities’ primary activities, they generally do not exert control over an investee. This improvement is effective for periods beginning on or after January 1, 2015 and the accounting changes that arise should be recognized retrospectively.

Bulletin C-9 “Liabilities, provisions, contingent assets and liabilities and commitments”- Bulletin C-9 provides that foreign currency advances should be recognized at the exchange rate prevailing on the date of the transaction; that is, at the historical exchange rate. Such amounts should not be modified by subsequent exchange fluctuations between the functional currency and the foreign currency in which the price of goods and services related to such advance payments are denominated. This improvement is effective for periods beginning on or after January 1, 2015 and the accounting changes that arise should be recognized retrospectively.

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Management estimates that the new FRS and the improvements to FRS will be immaterial. FRS D-3 requires to record in “Other comprehensive income” the amounts for previous services related to transitional assets, plan amendments and actuarial losses accrued for pension benefits, seniority premiums and other post-retirement benefits. The Bank’s management is in process of analyzing the required records and defining an action plan with respect to the adoption of this FRS.